

# **Public Private Partnership and the Challenge of Post-Contractual Balance: The Case of the Ghana Telecom and Water Company Contracts.**

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**A thesis submitted to  
The University of Birmingham**

**For the Degree of**

**DOCTOR OF PHILOSOPHY**

**Centre for Business Strategy and Procurement  
Business School  
The University of Birmingham  
April 2013**

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## **ABSTRACT**

The World Bank and other multi-lateral donor organisations are increasingly urging governments in developing world to engage the private sector under the banner of Public Private Partnership to manage their public utility infrastructure and service provision. However, the World Bank's enthusiasm for this private sector model as a solution to developing country infrastructure and financing problems is not the result of compelling evidence. This argument that the public sector may not be able to achieve post-contractual balance and achieve good supplier balance is tested using data from two case studies in Ghana: telecom and water sector under PPP. Semi-structured interviews were undertaken and documentary sources collected. The case studies provided evidence that the Ghanaian public sector failed to achieve post-contractual balance and good supplier performance.

The study concludes that PPP is not delivering the expected good value for money for the public sector and that Ghanaian public officials specifically should be cautious of their optimism that they have the ability to develop balance and obtain value for money from the private sector partners.

This study fills a gap in transaction cost economics literature that does not consider power as relevant in the outcome in business-to-business relationships. It contributes to literature by demonstrating that adverse pre-contractual power relation can act as a constraint on the public sector to develop post-contractual balance with the private sector.

Baba Iddirisu

## **DEDICATION**

To

Mum and Dad

## **ACKNOWLEDGEMENT**

This production of this thesis is the result of efforts of many people to whom I owe a great debt of gratitude.

I am foremost indebted to my primary supervisor Dr. C. Lonsdale and co-supervisor Dr .J Sanderson both of Strategy and Procurement Management at the Birmingham Business School, for his unfailing support and confidence in my research work. I thank him for his excellent supervision whose keen knowledge in public-private partnerships in UK was invaluable one for this project.

I also express my profound gratitude to J. Dr. Sanderson my co-supervisor for his tremendous support during my research work providing me with valuable comments on this research.

This thesis could not have been completed without practical information and logistic support from the two companies in Ghana. I am indebted to staff and workers at Ghana Water Company Limited and Vodaphone Ghana who offered me tremendous opportunity to interview them on such national sensitive matter.

Special thanks also go to Dr. G Dampare of Ghana Police for his support and encouragement during my research work.

I wish also thank staff and students of the Birmingham Business School, particularly those who helped me through the MBA and Doctoral work with unique experience.

Finally, I extend my special thanks to my parents for their endless love whilst on my studies. Their prayers have always been a great inspiration to me than words could ever describe.

# TABLE OF CONTENTS

<b>INTRODUCTION</b>	<b>1</b>
<b>CHAPTER 1</b>	<b>6</b>
<b>AN OVERVIEW OF THE LITERATURE ON PUBLIC PRIVATE PARTNERSHIPS</b>	<b>6</b>
1.1 INTRODUCTION	6
1.2 THE BENEFITS OF PPP TO THE PUBLIC SECTOR	6
1.2.1 EVIDENCE OF THE GROWTH OF PPP	9
1.2.2 DRIVERS OF THE GROWTH OF PPP	13
1.2.3 THE DRIVERS OF PPP GROWTH WITHIN DEVELOPING COUNTRIES	16
1.3 PPP AND RISK TRANSFER	18
1.5 EVIDENCE OF RISK ALLOCATION TO THE PUBLIC SECTOR.	23
1.6 PPP DEFINITION	32
1.6.1 INTRODUCTION	32
1.6.2 PPP DEFINITION	33
<b>CHAPTER 2</b>	<b>41</b>
<b>LITERATURE OVERVIEW OF BILATERAL GOVERNANCE</b>	<b>41</b>
2.1 INTRODUCTION	41
2.2 MODELS OF CONTRACT MANAGEMENT	42
2.2.1 AGENCY THEORY	43
2.2.2 PROPERTY RIGHTS MODEL	45
2.2.3 JUSTIFICATION OF TCE	46
2.3.1.1 BOUNDED RATIONALITY	52
2.3.1.2 OPPORTUNISM	53
2.3.1.3 THE SIGNIFICANCE OF THE BEHAVIOURAL ASSUMPTIONS	55
2.3.2 BILATERAL GOVERNANCE	64
2.3.3 EMERGENCE OF BILATERAL CONTRACTING IN BUSINESS RELATIONSHIPS	65
2.4.1 APPROACHES TO CONTRACT DISPUTES RESOLUTION	71
2.4.2 THE EXPECTATION OF BALANCE: BILATERAL GOVERNANCE SHARED INVESTMENTS OR USE OF FINANCIAL HOSTAGES	74
2.4.3 EVIDENCE PROVIDED BY TCE FOR BILATERAL BALANCE	77
2.5 CONCLUDING COMMENTS	78
<b>CHAPTER 3</b>	<b>81</b>
<b>POWER AND CONTRACTUAL BALANCE</b>	<b>81</b>
3.1 INTRODUCTION	81
3.1.1 GENERAL CRITICISMS OF TCE	81
3.1.2 INCENTIVE THEORIES AND PROCUREMENT FUNCTIONS	83
3.1.3 TCE ASSUMPTIONS ON CREDIBLE COMMITMENTS	85
3.2 TCE AND POWER	86
3.2.1 PRE-CONTRACTUAL POWER AND CONTRACTUAL BALANCES- LONSDALE FACTOR	90
3.2.2 IMPACT OF POWER ON SURPLUS VALUE	93
3.3 A MODEL FOR PPP BALANCE.	96
3.3.1 CAPABILITY AND RESOURCE OF THE BUYING FUNCTION	98
3.3.2 IMPORTANCE OF NEGOTIATION RESOURCE AND CAPABILITY	101

3.3.3 ATTRIBUTES OF A GOOD NEGOTIATOR	103
3.3.4 SUPPLIER PERFORMANCE	108
3.4 CONCLUSION	110
CHAPTER 4	111
THEORETICAL MODEL AND HYPOTHESIS	111
4.1 TOWARDS THE ANALYTICAL FRAMEWORK AND HYPOTHESES	111
4.2 PROBLEM STATEMENT	111
4.3 JUSTIFICATION OF GHANA CHOICE	115
4.4 HYPOTHESIS AND RATIONALE FOR THE STUDY	116
CHAPTER 5	119
METHODOLOGY	119
5.1 INTRODUCTION	119
5.2.1 EPISTEMOLOGICAL APPROACH TO THE STUDY	120
5.2.2 RESEARCH DESIGN	122
5.2.3 CASE STUDY	123
5.2.4 QUANTITATIVE VS QUALITATIVE	125
5.3 OPERATIONAL DEFINITIONS OF CONSTRUCTS	128
5.3.1 QUALIFYING VARIABLES	128
5.3.2 DEFINITIONS AND OPERATIONALISATION OF CONCEPTS	130
5.3.3 INDEPENDENT VARIABLES	130
5.3.4 DEPENDENT VARIABLE	140
5.3.4.1 HYPOTHESIS 1: DEPENDENT VARIABLE: POST CONTRACTUAL BALANCE	140
5.3.4.2 HYPOTHESIS 2: DEPENDENT VARIABLE: SUPPLIER PERFORMANCE	142
5.3.4.3 MEASURING INSTRUMENTS (MEASURES)	143
5.4.1 MEASURES USED IN PART OF THE SEMI-STRUCTURED INTERVIEW	144
5.4.2 MEASURES USED IN THE INTERVIEW QUESTIONS	145
5.4.3 PROCEDURES FOR INTERVIEW DATA COLLECTION.	148
5.4.4 PILOT STUDY	149
5.4.5 SOURCES AND EVIDENCE: SELECTING INTERVIEWS	152
5.5 INTERVIEW PROCESS	155
5.5.1 DOCUMENTARY SOURCES	156
5.5.2. DATA PROCESSING	158
5.5.3.1 OBJECTIVITY AND VALIDITY	161
5.6 CONCLUSION	163
CHAPTER 6	164
THE GHANA PPP CONTRACTS: GT AND GWCL	164
6.1 INTRODUCTION	164
6.2 THE GHANA AND PPP POLICY	165
6.2.1 FACTORS DRIVING PPP REFORMS	165
6.2.2 POLITICAL CONTEXT OF PPP REFORMS	167
6.3 THE 1980s: A DECADE OF DECAY AND DELAYS	168
6.3.1 GHANA TELECOM	168
6.3.2 THE GT CONTRACT WITH TELENOR PPP	172
6.4 GHANA URBAN WATER CONTRACT CASE	174
6.4.1 BACKGROUND TO THE CASE	174

6.4.2 MOVE TO THE MARKET	176
6.4.3 THE AVR L PPP	177
6.5 THE STRUCTURE OF THE TELECOMS AND WATER MANAGEMENT CONTRACTING OF PPP	180
CHAPTER 7	183
PRESENTATION OF INTERVIEW DATA	183
7.1.1 PRE-CONTRACTUAL POWER RESOURCES OF GT AND TMP	183
7.1.2 INDEPENDENT VARIABLES UTILITY –GT INTERVIEW DATA	184
7.1.3 SCARCITY: AVAILABLE OF SUPPLIERS	187
7.1.4. INFORMATION ON THE CONTRACT	190
7.2.1 SUPPLIER SIDE TMP	191
7.2.2 INTERVIEW AND OTHER DATA: NEGOTIATIONS AND RESOURCES AND CAPABILITIES	193
7.2.3 THE NEGOTIATION RESOURCES AND CAPABILITY OF GT AND TMP	193
7.3 ANALYSIS OF THE PRE-CONTRACTUAL POWER RELATIONSHIP	196
7.3.1 PRE-CONTRACTUAL POWER ANALYSIS:	197
7.3.2 ANALYSIS OF FACTORS RESOURCE AND NEGOTIATION CAPABILITIES	202
7.3.3. CONCLUSION	205
7.4 ANALYSIS POST-CONTRACTUAL IMBALANCE	206
7.4.1 RISK SHARING: FIXED ASSETS	207
7.4.2 RISK SHARING IN THE CONTRACT: COST PLUS INCENTIVES	209
7.4.3 SOVEREIGN GUARANTEES AND SWITCHING COSTS.	212
7.4.4 CONTRACT INFLEXIBILITY AND POST-CONTRACTUAL-RENEGOTIATION	213
7.4.5 INFORMATION AND MORAL HAZARDS:	215
7.5.1 INDEPENDENT VARIABLES : PRE-CONTRACTUAL DATA	220
7.5.2 SCARCITY: SUPPLIER AVAILABILITY	222
7.5.3 INFORMATION ON THE CONTRACT	224
7.5.4 SUPPLIER SIDE: UTILITY	225
7.5.6 SUMMARY	226
7. 6 ANALYSIS OF THE PRE-CONTRACTUAL POWER RELATION BETWEEN GWCL AND AVR L	227
7.6.1 ANALYSIS OF FACTORS RESOURCE AND NEGOTIATION CAPABILITIES	234
7.6.2 THE NEGOTIATION RESOURCES AND CAPABILITIES OF GWCL AND AVR L	235
7.7 CONCLUSION:	240
7.7 POST –CONTRACTUAL BALANCE: THE EVIDENCE	240
7.7.1 RELEVANCE OF RISK AND UNCERTAINTY IN THE WATER SUPPLY SECTOR AND MANAGEMENT	241
7.7.2 RISK SHARING: FIXED ASSETS	244
7.7.3 RISK SHARING;; CONTRACT COST AND INCENTIVE	245
7.7.4 INFORMATION ASYMMETRY	246
7.7.5 SOVEREIGN GUARANTEE AND HIGH SWITCHING COST	247
7.7.6 CONTRACT RIGIDITY AND CONTRACT RENEGOTIATION	247
CHAPTER 8	251
DEPENDENT VARIABLE: SUPPLIER PERFORMANCE	251
8.1 INTRODUCTION	251
8.1.1 REVIEW OF TMP’S PERFORMANCE DURING CONTRACT PERIOD	251
8.1.2 FINANCIAL PERFORMANCE	255
8.2 DISCUSSION	258
8.3.1 REDUCTION OF UNACCOUNTED WATER LOSSES	263
8.3.2 COST OF OPERATIONS	270
8.4 CONCLUDING REMARKS	274



<b>CHAPTER 9</b>	<b>277</b>
<b>CONCLUSIONS AND CONTRIBUTIONS</b>	<b>277</b>
<b>9.1 INTRODUCTION</b>	<b>277</b>
<b>9.2 PURPOSE OF THE STUDY AND HYPOTHESIS</b>	<b>277</b>
<b>9.3 SUMMARY OF FINDINGS</b>	<b>279</b>
<b>9.4 DISCUSSIONS</b>	<b>280</b>
<b>9.5 PPP-MANAGEMENT CONTRACTING</b>	<b>288</b>
<b>9.6 CONTRIBUTION</b>	<b>289</b>
<b>9.6.1 THEORY</b>	<b>290</b>
<b>9.6.2 CONTRIBUTION TO PRACTICE</b>	<b>291</b>
<b>9.6.3 RECOMMENDATIONS FOR IMPROVEMENT</b>	<b>293</b>
<b>9.7 LIMITATIONS</b>	<b>294</b>
<b>9.7.1 FUTURE RESEARCH</b>	<b>298</b>
<b>9.7.2 CONCLUDING REMARKS</b>	<b>300</b>
<b>APPENDIX A.</b>	<b>302</b>
<b>APPENDIX B</b>	<b>320</b>
<b>REFERENCES</b>	<b>321</b>

## FIGURES

FIGURE 1.1 PPP PROJECTS: WORLD BANK PROGRAMME .....	12
FIGURE 2.1 FRAMEWORKS FOR TRANSACTION COST ANALYSIS .....	51
FIGURE 2.2 CONTRACTING IN THE CONTEXT OF BOUNDED RATIONALITY AND OPPOTTUNISM .....	55
FIGURE 3.1 FRAMEWORK FOR ASSESSING THE SCOPE FOR RISK TRANSFER .....	88
FIGURE 3.2 THE FOUR STATES OF PRE-CONTRACTUAL POWER RELATION .....	93
FIGURE 3.3 GENERIC BUYER AND SUPPLIER RELATIONSHIP TYPES .....	94
FIGURE 4.1 THE THEORETICAL MODEL FOR THE RESEARCH .....	113
FIGURE 6.1 TRIPARTITE RELATIONSHIPS IN THE TELECOMS AND WATER CONTRACTS .....	181

## LIST OF TABLES

<b>TABLE 1.1 PFI SIGNED DEALS IN UK .....</b>	<b>10</b>
<b>TABLE 1.2 PPP PROJECTS IN EUROPE .....</b>	<b>11</b>
<b>TABLE 1.3 RISK ALLOCATION IN PPP .....</b>	<b>22</b>
<b>TABLE 1.4 PFI AND COST OVERRUNS .....</b>	<b>24</b>
<b>TABLE 1.5 COST SAVINGS IN PPP .....</b>	<b>27</b>
<b>TABLE 2.2 SUMMARY OF ORGANISATION CHOICES AND BALANCE .....</b>	<b>77</b>
<b>TABLE 5.1 FRAMEWORK FOR THE SPECIFICATION AND MEASUREMENT OF THE VARIABLES .....</b>	<b>132</b>
<b>TABLE 5.2 FRAMEWORK TO DETERMINE THE PRE-CONTRACTUAL POWER RELATION .....</b>	<b>136</b>
<b>TABLE 5.3 FRAMEWORK TO DETERMINE THE RELATIVE RESOURCES AND CAPABILITIES IN NEGOTIATIONS .....</b>	<b>139</b>
<b>TABLE 5.4 APPROACHES TO DATA COLLECTION AND ANALYSIS .....</b>	<b>151</b>
<b>TABLE 5.5 CODES FOR THE INTERVIEWEES .....</b>	<b>153</b>
<b>TABLE 5.6 NUMBER OF INTERVIEWEES .....</b>	<b>154</b>
<b>TABLE 5.7 LIST OF DOCUMENTS ANALYSED .....</b>	<b>157</b>
<b>TABLE 6.1 BASIC TELECOMMUNICATIONS NETWORK INDICATORS .....</b>	<b>169</b>
<b>TABLE 6.2 SOURCE OF FUNDING FOR STP IN MILLION USD .....</b>	<b>170</b>
<b>TABLE 7.1 SUMMARY OF FINDINGS FOR GT INTERVIEWS .....</b>	<b>ERROR! BOOKMARK NOT DEFINED.</b>
<b>TABLE 7.2 SUMMARY OF FINDINGS FOR TMP (SUPPLIER) .....</b>	<b>ERROR! BOOKMARK NOT DEFINED.</b>
<b>TABLE 7.3 SUMMARY OF RESULTS: PRE-CONTRACTUAL ANALYSIS OF GT AND TMP .....</b>	<b>ERROR! BOOKMARK NOT DEFINED.</b>
<b>TABLE 7.4 SUMMARY OF INTERVIEWS ON NEGOTIATION RESOURCES AND CAPABILITIES .....</b>	<b>203</b>
<b>TABLE 7.5 MAPPING THE RESOURCES AND CAPABILITIES OF NEGOTIATIONS .....</b>	<b>204</b>
<b>TABLE 7.6 SUMMARY OF RESULTS: PRE-CONTRACTUAL ANALYSIS OF GWCL AND AVRL .....</b>	<b>228</b>
<b>TABLE 7.7 SUMMARY OF RESULTS OF GWCL INTERVIEWS .....</b>	<b>229</b>
<b>TABLE 7.8 SUMMARY OF RESULTS OF AVRL INTERVIEWS .....</b>	<b>230</b>
<b>TABLE 7.9 SUMMARY OF NEGOTIATION RESOURCES AND CAPABILITIES IN NEGOTIATIONS OF GWCL AND AVRL .....</b>	<b>238</b>
<b>TABLE 8.2 COMPARISON OF TMP AND AREEBA FINANCIAL PERFORMANCE .....</b>	<b>257</b>
<b>TABLE 8.3 GWCL AND AVRL PERFORMANCE 2006-2009 .....</b>	<b>263</b>
<b>Table 8.4 Key Performance Benchmarks .....</b>	<b>264</b>

## **ABBREVIATION AND ACRONYMS**

<b>ADP</b>	<b>Accelerated Development Plan</b>
<b>AVRL</b>	<b>Aqua Vittens Rand Limited</b>
<b>BOT</b>	<b>Build Operate Transfer</b>
<b>GP&amp;T</b>	<b>Ghana Post and Telecommunication</b>
<b>GT</b>	<b>Ghana Telecom</b>
<b>GWCL</b>	<b>Ghana Water Company Limited</b>
<b>HIPC</b>	<b>Heavily Indebted Poor Countries</b>
<b>IFC</b>	<b>International Finance Corporation</b>
<b>IMF</b>	<b>International Monetary Fund</b>
<b>MDGs</b>	<b>Millennium Development Goals</b>
<b>MIGA</b>	<b>Multilateral Investment Guarantee Agency</b>
<b>NAO</b>	<b>National Audit Service</b>
<b>NCA</b>	<b>National Communication Authority</b>
<b>NPM</b>	<b>New Public Management</b>
<b>OPIC</b>	<b>Overseas Private Investment Corporation</b>
<b>PAC</b>	<b>Public Accounts Committee</b>
<b>PPP</b>	<b>Public Private Partnership</b>
<b>PFI</b>	<b>Public Finance Initiative</b>
<b>PURC</b>	<b>Public Utility Regulatory Commission</b>
<b>STP</b>	<b>Second Telecom Project</b>
<b>TCE</b>	<b>Transaction Cost Analysis</b>
<b>TI</b>	<b>Transparency International</b>
<b>TMP</b>	<b>Telenor Management</b>
<b>TNOs</b>	<b>Trans-National Organisation</b>
<b>UN</b>	<b>United Nations</b>

## INTRODUCTION

The world is being ushered into new era of partnership arrangements for delivering a variety of public services on behalf of governments. A form of partnership that has been receiving a great deal of attention in recent years is the Public-Private Partnership (PPP). PPP is a form of business arrangements between the state and the private sector entities to deliver public goods, services and infrastructure (HM Treasury, 2003b; European Investment Bank, 2007; World Bank, 2011). Notably, most governments in developed and developing countries have applied public-private policy in public provision. In its early development especially during post-World War period governments in the USA and some Europe countries used the private sector to mobilise resources for national constructions. However, PPP initiatives in public provision were given a political legitimacy by the then Thatcher administration in the 1980s. Under the banner of Private Finance Initiatives (PFI)<sup>1</sup>, the UK conservative was able to tap into the pool of private finance to provide under-supplied key public infrastructure and services in education, health, transport and defence (The Stationary Office, 2000; Akintoye et al., 2003; Broadbent and Laughlin, 2005; Julius, 2008; Oxford Economics, 2008).

There is growing evidence in the literature that suggests that the PPP brings about several benefits to the governments. It is claimed that public sector benefit from access to private sector financing, cutting-edge technology, innovation and project management competences.

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<sup>1</sup> The term Private Finance Initiative (PFI), though not fundamentally different from PPP, is commonly used to refer to private sector initiatives. Under UK PFI arrangements, the private sector finances the project and sells it to the public sector. In return the public sector commits itself to make future payments to the private sector over a stated period. Unless a distinction is made, PPP in this thesis refers also to PFI.

More importantly, a greater part of the literature claims that PPP affords the public sector a convenience medium to transfer project risk.

In the UK, the confidence of transferring project risk is illustrated by the growing use of private finance to fund public infrastructure. Official figures show that by 2003, a total of 570 PFI contracts had been signed, with an estimated value of £36 billion (OGC, 2003; HM Treasury, 2003a). These included 119 health schemes and 239 refurbished schools (HM Treasury, 2003b; Broadbent and Laughlin, 2005). By March 2006, private financed projects had been extended to prisons, bridges, hospitals, roads, and military installations with a capital value around £50 billion.

In continental Europe, studies indicate that PPP policy in public sector infrastructure provision is becoming increasingly popular with Spain establishing itself as the second largest market in terms of volume and value. According to an EIB report, by 2006 a total of 92 public projects had been signed, representing a capital value of almost 200 billion euro (European Investment Bank, 2007; Blanc-Blude et al., 2007; Julius, 2008).

In the USA, the PPP model had been used by the Federal government since the 1950s as an economic tool for stimulating private investment (Schneider, 1999; Bult-Spiering and Dewulf, 2006). In recent times, sensitive public projects in social works, education, prisons, and transport add to the growing list of public services that the Federal government is using the private sector to provide. Schrank and Lomax (2005), for example, report that PPP funded

projects in the US over the past decade in the transport sector alone are estimated at a value of \$463.1 billion.

In contemporary times, PPP initiatives have also started to emerge in Sub-Saharan Africa and other parts of the developing world as a response to infrastructure gap in public utilities and inadequate budgetary funding. At the centre of PPP emergence in Sub-Saharan Africa is the over bearing influence of the World Bank. The World Bank is using a broad and diverse set of policies including persuasive and coercive funding conditions to force governments especially in African countries to introduce drastic public procurement reforms to accommodate the private sector in public service delivery. Recent figures show that the World Bank, IMF and other multi-lateral lending agencies have increased their financial and technical assistance considerably to fund PPP projects. For example, the World Bank investment package for PPP projects in developing countries for the next 25 years stands at between US\$75 billion and US\$180 billion (World Bank, 1997, 2003b; Finger and Allouche, 2002; Smith and Hanson, 2003). According to a more recent report released in 2011, the World Bank has spent about US\$ 12 billion on various PPP projects in several African and Asian countries (World Bank, 2011).

Despite the above-mentioned positive contributions of PPP to national development and its increasing appeal among policy makers, multi-lateral funding institutions and governments, the implementation of the public-private sector business model comes with much controversy. A number of studies demonstrate that the public sector had not been able to transfer risk to the private sector and that PPP model has not delivered cost savings as expected (Hartley and Parker, 2003; Bovaird, 2004; Lonsdale, 2005a; Lonsdale and Watson, 2007). It is typically

argued that it is difficult for UK public sector authorities to negotiate effectively for better deals with profit seeking private sector because of risk and uncertainty associated with transacting with external third parties over long term contracts (Cox et al, 2001; Lonsdale, 2005).

However, the controversy over the balance debate in PPP literature, appear to rest on prescriptions given by Williamson in his transaction cost framework (1983, 1986). Transaction cost economics theory (TCE) which is primarily concerned with how buyers and suppliers manage their contract relation to achieve cost efficient outcomes retains the confidence that buying organisations have the ability to anticipate risk and craft credible commitments to balance risk (Williamson, 1983; 1996). While TCE claims to post-contractual balance using credible commitments cannot be denied, it has been pointed out that there are some factors that may make it practically difficult for the public sector to do so successfully. Looking at this issue in more detail, the main factors that are said by some to impair the ability of public authorities to achieve contractual balance with their private sector partners are two-fold: Pre-contractual power relations (which constrain the ability of public authorities to commit the private partner in negotiations to contractual balance (Cox et al., 2000; Lonsdale, 2005a; 2005b) and the asymmetry in resources and negotiation capabilities of the contracting authorities (which can lead to the public authorities being ‘outplayed’ during the negotiations by their private sector partners, which again leads to an unbalanced contract (Lonsdale, 2005b; Vigoda and Kapun, 2005; Cook and Aryee, 2006).

In order to investigate the above arguments, this thesis looked at two PPPs companies run by the Ghanaian government – Ghana Telecom and Ghana Water Company – aiming at



providing new evidence on Lonsdale's arguments to contribute to the debate on PPP. To facilitate this, and given the complexity of the PPP policy in public procurement management, a major consideration is given to alternative theories of TCE, agency, property rights which may inform the analysis with the aim of firstly evaluating and extending theory and secondly to identify its implications for future PPP practice in Ghana.

This thesis is organised into 9 chapters. In Chapter 1, the author reviews the broader PPP literature. This provides the theoretical context to the review of the literature concerning bilateral governance and balance in Chapter 2. The main developments of theoretical framework for contract management and argument of each approach are reviewed. With that, justification was provided for the choice of TCE framework for the research and the chapter proceeds to review the literature on general contracting problems and solutions based on incentive contracting economics theories. Chapter 3 provides theoretical analysis of TCE critique in the context of contractual problem of post-contractual balance problems through the lens of resources and power dependent theories. Chapter 4 develops on the previous chapters review, draws the theoretical framework for the empirical study and outlines the hypotheses. Chapter 5 deals with the research methodology for the research and lays out the philosophical assumptions, the research methods and the justification for using a qualitative case study. Chapters 6 provide a profile of the contracting environment of PPP in Ghana. In Chapter 7 the empirical data of the two cases are presented and analysed. Chapter 8 analyses the impact of the post-contractual imbalance on supplier performance. Finally, Chapter 9 concludes the study. The results of the two cases and the post-contractual power structure and the relevance of the TCE approach to post-contractual balance are summarised and the contributions it has made to knowledge and practice. It finally outlines areas for further research.

# **CHAPTER 1**

## **An Overview of the Literature on Public Private Partnerships**

### **1.1 Introduction**

PPP has been the subject of intense academic research over the past two decades in examining its effectiveness in the area of creating conditions for developing mutual-inter-dependency with the private sector and delivering value for money. In this chapter, the author reviews the resultant literature in order to set the stage for an extended review of TCE contractual solutions to protect economic actors in exchange relationships to be discussed in later chapters.

Discussions in this chapter are organised as follows. Section 1.2 discusses the benefits and growth of PPP in both developed and developing countries. In Section 1.3, the author reviews the perceived reasons for the growth in PPP both in developed and developing countries. In Section 1.4, the author reviews the claims and counter-claims that have been made for PPP, with respect to risk transfer and cost efficiency. Finally the author reviews of PPP definition in section 1.6 and with the aim of adopting a working definition for this study.

### **1.2 The Benefits of PPP to the Public Sector**

There is growing evidence in the strategic management and marketing literature that suggests that partnerships bring about benefits to parties in many ways (Grimsey, and Lewis, 2007;

Thomsen and Steets, 2009). These broad benefits include risk transfer opportunities, early project completion times and on budget, access to private sector technology and innovation; scope for sharing knowledge and competences. In addition to the above benefits, the public sector is expected to gain access to private sector funding for key public projects government budgetary constraints affect their early take off. Some writers (e.g. Thomsen and Steets, 2009) contend that PPP provides the impetus for organisational reforms and institutional innovation. These reforms that had allowed managers within the public sector to take on market principles are believed helping them to improve upon their project planning and management skills. Studies in the strategic and management literature also show that public sector managers working with the private sector on public projects have acquired valuable skills in setting achievable targets and budgetary control planning, a knowledge that been utilised effectively in other areas of public management (see Spackman (2002; NAO, 2003a). For example, Spackman (2002) found that PPP has helped in producing clear objectives, new ways of planning projects, and incentives for competitive tendering. PFI-based procurement has also forced NHS managers to concentrate more on outcomes than inputs, thus increasing efficiency (Pollock et al., 2001). The UK National Audit Office (NAO) report claimed that collaboration with the private sector has enabled the UK government to achieve its primary objectives of providing efficient services and that private funding of public sector projects brought a number of benefits in the form of shorter project times and greater reliability (NAO 2003a).

There are other intrinsic benefits from public-private working relationships, particularly in the IT sector. Studies in the UK showed that the public sector has utilised private sector expertise in ICT in many areas of government business, harmonising e-commerce across public departments from the procurement function to the creation of databases for all types of

government e-business transactions. This is significant development in UK public sector e-commerce government's business by allowing different public sector organisations to share relevant information across government bodies and harmonise their functions through shared databases for consistent applications of government policies something which was difficult to do previously. The Benefits Agency (UK Treasury Taskforce, 1999) and the Inland Revenue (NAO, 2003e, PAC, 2003b) and the Offender Register Database (PAC, 2009) are a few of the areas that have benefited from PFI schemes.

This is by no means an exhaustive list but it they provide a wide representative view of the various benefits accrued to governments working closely with the private sector not only in UK but possible in other countries as well. While empirical evidence shows that there is benefit in collaboration particularly PPP private sector involvement in public provision also comes with risk of losing autonomy and control which would be discussed later in the chapter.

Turning our attention to PPP, several studies show that the policy now assumes a greater importance in many national development agendas. Bovaird (2004) found that PPP forms an integral part of economic and industrial programmes in some countries, for example Italy and France. In the USA, PPP has become a major part of its urban development policy. Various studies also point to examples of partnerships in developing countries that are increasingly becoming an integral part of their national development agenda, such as in South Africa, some south eastern Asian countries and Latin America (Smith and Hanson, 2003). Multilateral lending institutions have also adopted PPP as part of their strategic documents. In Ghana, for example, PPP is being integrated into the national development plan to provide public infrastructure development under the MDGs.

It is important to point out that PPP is different from privatisation, even though many writers consider it as a disguised form of privatisation (Sheil, 2002). Whilst privatisation typically involves the complete transfer of state ownership of a public facility to a private business entity, PPP allows the state to retain ownership and control (Grout, 2002; Bovaird, 2004). Similarly, contracting out that involves outsourcing a service to private contractors, for example cleaning or security is distinct from PPP (Boyne, 1998; Wooldridge et al., 2002; Christensen & Pallensen, 2004). However, discussions about the merits of both privatisation and contracting out are outside the scope of this thesis.

### **1.2.1 Evidence of the Growth of PPP**

Although PPP is widely practised worldwide, it is difficult to obtain exact information on the real growth of PPP in terms of numbers and value (Estache et al., 2007; DLA Piper, 2007). This is due in part to the confusion over the distinction between PPP and other contracting out schemes. In the UK, available statistics exist, but as Schrank and Lomax (2005) pointed out definitional problems of PPP mean that some projects are excluded from the compilation of PPP projects<sup>2</sup>. Elsewhere, outside the UK, it is even more difficult to obtain reliable data on PPP, especially in developing countries where there is a considerable grey area between full privatisation and PPP (Schrank and Lomax, 2005).

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<sup>2</sup>The latest PFI signed deals data published by HM Treasury in July 2007 lists 582 projects (See [http://www.hm-treasury.gov.uk/documents/public\\_private\\_partnerships/ppp\\_pfi\\_stats.cfm](http://www.hm-treasury.gov.uk/documents/public_private_partnerships/ppp_pfi_stats.cfm)). However, they state that this list omits many deals previously reported by line Ministries, due to their being either completed, consolidated or smaller than the revised recommended PFI/PPP threshold of 30million euro. The Partnerships UK projects database lists 816 projects for the same period, of which 670 are operational (see: <http://www.partnershipsuk.org.uk/ProjectsDatabase/projects-dbase.asp>).

Despite this difficulty, the few existing statistics give us a broad view of the growth of PPP worldwide. In the UK, for example, data from the Office of Government Commerce (OGC) shows that by 2003 there were about 570 PPP/PFI projects in the UK with an estimated value of £36 billion. Out of these, about 60 per cent of the value went to the Department of Transport, with the Department of Health accounting for nearly £3 billion (Office of Government Commerce 2003). This number has steadily increased over the years to about 812 projects by the end of 2006, with average new signings of between 90 and 100 projects annually (European Investment Bank, 2007). Details of PFI signed deals and values can be seen in Table 1.1

**Table 1.1 PFI Signed Deals in UK**

	Number	£ million
Transportation	36	20,526
Health	126	2, 891
Defence	45	2,359
Scotland	80	2, 092
Education and Skills	93	1 858
Home Office	44	1,767
Work and Pensions	7	930
Inland Revenue	10	491
Wales	26	439
Northern Ireland	28	366
Environment, Food and Rural Affairs	11	349
GCHQ	1	330
ODPM	27	302
Lord Chancellor's Departments	11	256
Trade and Industry	9	194
Treasury	1	118
Foreign and Commonwealth Office	2	91
Customs & Excise	2	83
Northern Ireland Court Service	2	65
Culture, Media and Sport	3	44
National Savings	1	37
Cabinet Office	1	12
Office of Government Commerce	1	10
Public Record Office	1	-
<b>Total</b>	<b>568</b>	<b>35,610</b>

Source: Office of Government Commerce Data, 2003

The European Investment Bank (EIB), one of the major financiers of PPP infrastructure projects in Europe, reports significant growth of PPP across continental Europe. Their latest released statistics (EIB, 2007) showed that the 15 years up to 2006 witnessed significant growth of PPP, with more than 1,000 contracts signed in the EU, representing a capital value of £200 billion euro as depicted in Table 1.2 below

**Table 1.2 PPP Projects in Europe**

Year	Number of signed projects	Value of signed projects (Euro millions)
1993	1	454
1994	2	268.1
1995	15	3277
1996	31	8420.1
1997	42	5268.5
1998	79	19965.8
1999	86	9707.3
2000	106	15746.3
2001	83	152192.2
2002	89	20521.1
2003	99	18461.3
2004	135	18124.5
2005	137	28768.1
2006	152	28427.2
TOTAL	1066	194711.6

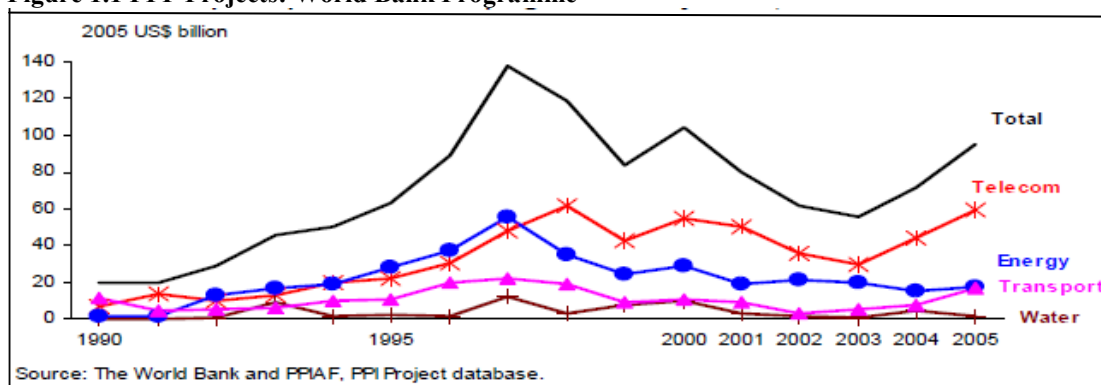
Source: EIB 2007

In the US, where PPP has been practised for several decades immediately after the end of the second world war substantial growth in private sector participation in public infrastructure development and service delivery have been reported (McDonough, 1998). According to MacNeil and Warnock (2000) several thousands of housing units were developed through PPP in the 1990s in the US. Other services like solid waste disposals, ambulances and

correctional facilities are also said to be provided by public private arrangements (Bloomfield, 1998; McDonough, 1998).

In Africa and other parts of the developing countries PPP procurement policy is gaining popularity among governments seeking external funding to key public infrastructure development and services. Figure 1.1 compiled by Estache, et al. (2007) from various databases, shows an amount of US\$1000 billion committed to PPP projects between 1990 and 2005 under World Bank payments. By 2010, US\$71.26 billion is reported to have been spent (World Bank, 2011). In 2010, the World Bank is said to have spent US\$2.3 billion on water infrastructure and supply services and a further US\$11.9 billion on telecommunications (World Bank, 2011).

**Figure 1.1 PPP Projects: World Bank Programme**



The above examples illustrate the growing influence of PPP both in numbers and value but what accounts for its growth. In the next section, we examine some of the principal factors responsible for PPP growth as alternative to traditional public procurement.



### **1.2.2 Drivers of the Growth of PPP**

As already noted, PPP is acknowledged by many writers to be a mechanism for providing opportunities to governments to achieve their infrastructure and service targets. Criticisms of state monopoly and bureaucracy in the management of public utilities have led to the redefinition of the role of the state within market-led ideology. The rationale behind this paradigm shift is to encourage competition between service providers, share risk and drive costs down for the benefit of the public (Osborne and Gaebler, 1992). Beyond this broad rationale, several factors have been identified to account for the sudden explosion of PPP, both in the developing and developed countries. These are summarised as follows.

The first factor behind the rise of PPP was the growing realisation that the public sector could not shoulder all of the state obligations alone (Bovaird, 2004). For example, since the 1980s, successive UK Labour and Conservative governments, despite their ideological differences, have consistently used the private sector funding and innovation to close infrastructure gap in health, schools, roads, defence that their tight budget could not provide funding upfront (see also Parker and Hartley, 2003; Grahame, 2003). Moreover, payment for these services are spread over several years some lasting more than 20 years. As was argued by Froud (2003) this has not only freed the UK government from pressure to finance projects from its own resources, but also helped the government to keep national debts low in the balance sheet called 'off balance sheet financing' (Spackman, 2002; Grahame, 2003; Dewatripont and Legros, 2005; Sadka, 2006). Off balance sheet financing refers to accounting arrangements where UK government's yearly payments made against private funded projects disguised as recurrent expenditures instead as long term loans. The advantage to the government is that its

true debt portfolio is hidden from the watchful eyes of credit rating agencies and the country continues to benefit from low borrowing interest rate (Dewatripont and Legros, 2005).

Second, it is contended that PPP offers governments the opportunity to transfer project risks to the private sector, something that is claimed to improve both service delivery and cost efficiency. Risk sharing and allocation goes to the heart of PPP ideology and arguably remains the singular key reason that informed Major's government's decision to launch the PFI in the UK back in 1992. The expectation that the risk would be transferred to the private sector however, is a normative presumption which this thesis addresses further in the study within the context of TCE framework.

Third, partnership advocates contend that PPP offers the public manager the opportunity to utilise private sector expertise and innovation, particularly in the high-tech construction and IT sectors (Osborne and Gaebler, 1992; Porter, 1995). It is argued that the traditional procurement system is wasteful and inefficient and that the introduction of market competition will not only drives cost down but will enable governments to tap into innovative ideas and market thinking into public administration. This argument is primarily based on neo-liberal logic that paradigm shift from traditional public sector management, which is deemed inefficient, to the private sector management, considered efficient, is capable of responding to the needs of the people in a most cost-effective way (Osborne and Gaebler, 1992; Porter and Dewey, 1998; Bevir and Rhodes, 2003). Neo-liberal thinkers argue that, by removing state control over public utilities and encouraging competition will reduce bureaucratic inefficiencies and the resulting savings passed onto consumers and tax payers

(see Boyne, 1998; Buse et al., 2005). Thus the private sector efficiency philosophy has come to dominate current thinking in the public sector.

Fourth, it is not just governments that have been converted to the idea of PPP. A growing part of literature in developing countries suggests international development agencies like the IMF, the World Bank and various UN agencies have been at the forefront of encouraging and coaxing governments to adopt the private sector as development partners (Alexander, 2002; Kessler, 2004). In the case of the World Bank, it has gone beyond policy rhetoric and incorporated the principles of private sector participation in its policy documents, something that accounts for the growth of PPP in developing countries albeit, lending conditions.

None of the above factors would have been of any significance, however, if the private sector had not been willing to accept project and service risks under PPP, although the extent of the risk they are prepared to take on is a matter of debate; a debate that is at the heart of this thesis. The private businesses have increasingly come to appreciate the benefits of partnering with the public sector for new market opportunities and wealth creation (Julius, 2008). It is typically argued that Governments are usually the biggest aggregate spender in any economy, initiating high-capital projects for the provision of health, education, transport, IT and many other high profile public projects for their citizens (Cabinet Office, 1999; Estache et al., 2007). Julius (2008), for example, stated that the UK government spent an estimated £79.4bn in 2008 on services alone, representing 5.7% of GDP.

Beyond the UK, according to World Bank estimates, the PPP market has an estimated annual value of \$10 billion (Estache et al., 2007; World Bank, 2008). Projections from the World Bank also indicate a positive trend in market growth for the next ten years, as governments in Africa are expected to rely on the private sector to play a dominant role in providing public infrastructure and services for its increasing population (see, for example, Bayliss, 2002; Sadka, 2006). Not surprisingly, the private sector sees PPP as a huge opportunity to obtain lucrative government contracts and possibly lobbying and encouraging the PPP policy (Pollock et al., 2002). This suggests that the state is seen as a major source of business for the private sector and therefore increasingly attracting business interests and lobbying.

However, it could also be argued from another perspective that the influx of partnership in public sector provision is a response to pressure from the business community to open the public sector for private participation. Schaferhoff et al, 2007 argues that partnerships are serving business interests. However, these observations indicate business interests may prevail but that does not mean partnerships are meant to service business interests only. As has been discussed earlier, governments are benefiting from collaborating with the private sector. Clearly the relationship between business commercial interests and public welfare interests that calls into question the genuineness of the public sector interests.

### **1.2.3 The Drivers of PPP Growth within Developing Countries**

The growth factors discussed in the preceding section also apply to the increasing number of PPP-led projects in developing countries (Aryee and Cook, 2003). However, this is not the whole story. The rapid growth of PPP in developing countries is largely driven by the World

Bank's deliberate policy to tie large capital-based contracts in developing countries to private sector participation (Castro, 2002; Lobina and Hall, 2003; Aryee and Cook, 2003; World Bank 2006; Fobil et al., 2008).

One explanation is that most governments in developing countries face internal political pressure not to implement any economic reforms that will bring the private sector to manage public utilities for fear of economic exploitation. The other reality is that most governments are confronted with infrastructure gap and poor services and without private sector support would not be able to cope with increasing public demand for public infrastructure and improved services. In some instances a new infrastructure is required and in some cases more financial assistance to rehabilitate deteriorating ones. That is to say governments in developing countries needed external funding to embark upon their ambitious national reconstruction. Ghana for instance, is faced with a huge infrastructure gap averaging US\$1.5 billion per annum for the next decade. This is required to bring the nation's infrastructure to the recommended status of a middle-income country but has not got the needed resources.

However, the World Bank realised that despite the infrastructure gap that confronts developing countries and the difficulties of raising funds internally, most governments were not willing to involve the private sector for variety of reasons and the major is fear of private sector exploitation. On the other hand, the World Bank and its major contributors are determined to effect the needed changes to allow the private sector to bring in a new way of managing public infrastructure. Against this backdrop the World Bank seized any possible opportunity and using their loan facilities as a form of a carrot and a stick to persuade or

coerce unwilling African governments to involve the private sector as partners in national developments (Cassen, 1994; Finger and Allouche, 2002; World Bank, 2003a).

However, the involvement of the World Bank in PPP, has not only created uncertainty surrounding the PPP projects in developing countries in general and in Ghana in particular, but has generated a number of significant problems especially in designing balanced contracts with the private sector. This shifts our attention to examine the strategies the rationale behind PPP from the public sector perspective on trade-off between risk and efficient outcomes. In the next section we explore the concept of risk transfer and discuss why the concept is complicated and controversial in the management of PPP.

### **1.3 PPP and Risk Transfer**

There have been general discussions about measurement problems on PPP performance and outcomes. In particular, attempts to measure PPP performance across sectors have run into methodological difficulties as benchmarks and objectives differ from project to project, making any assessment unreliable for comparison purposes (Arthur Anderson Enterprise LSE 2001). Early assessments were largely based on cost-benefits analysis but that requires the development of clear industrial benchmarks by which the partnership in question can be evaluated. While it is easy to identify project cost assuming market prices apply, it has been found practically difficult to reduce public intrinsic benefits of service availability and satisfaction into verifiable figures. Moreover, the multi multi-faceted nature of PPP makes it increasingly becoming difficult to adopt an encompassing methodology to measure every aspect of PPP contribution to economic efficiency. As a result of these difficulties, the

traditional cost-benefits analysis often used contracting out literature are not vigorously applied to PPP projects (Grout 1997).

In the midst of this controversy emerged the use of risk transfer, which incidentally is the rationale behind PPP. The use of risk transfer to measure project success in terms of cost savings is universally accepted and is believed overcomes the weaknesses of other systems (Hartley and Parker, 2001; Pollock et al., 2002; Geddes, 2005). The UK HM Treasury (1995) refers to risk transfer as a key measure of value for money outcomes for the public sector. Indeed, some writers like Grout, 1997; Hartley and Parker, 2001; Pollock et al, 2001a) continually refer to risk transfer as a key test for value for money.

It is important to observe that risks transfer construct has empirical importance, as it allows PPP outcomes to be measured in terms of cost minimisation. Additional advantage to the public sector is that the use of risk transfer avoids the inconsistency and controversy over the comparison one outcome with another using different metrics (HM Treasury, 1995; Grahame, 2003). Arthur Anderson Enterprise LSE commissioned by UK Treasury Taskforce to examine the value for money aspects of PFI project put risk transfer ahead of other six output-based specifications competition, performance measurement and incentives, private management skill (Arthur Anderson Enterprise LSE 2001). The contribution of Arthur Anderson Enterprise LSE (2001) report is that risk transfer has now become the key rationale behind the public sector partnering with the private sector (HM Treasury, 1995; Pollock et al., 2001; Froud, 2003).

Subsequent studies have also established a link between risk transfer and value for money (see Spackman, 2002; Froud, 2003; Pollock et al, 2004; Shaoul, 2008). For example, Arndt

(1999) suggested in his work that the appropriate transfer of risks helps the public sector to achieve good value for money. Pollock (2004) used risks transfer to measure the degree of the benefits that the public sector is expected to obtain from the private sector. Others, like Vining et al. (2005) and Leahy (2005) also use risk transfer to draw a distinction between PPP and traditional procurement practices, and postulate that value for money is achieved where appropriate risks have been transferred.

Similarly, the World Bank uses the relationship between risk transfer and efficiency to emphasise that whether PPP ‘performs better than full provision by state-owned enterprises, depends, in particular, on whether performance risk is effectively shifted from taxpayers to the private shareholders of the company’ (World Bank, 2002: 23-24).

The above discussions illustrate risk transfer general acceptability as the key determinant of value for money in PPP projects but this also generates a significant debate as to whether the public sector have in the past transferred risk or have the ability to pass the appropriate risk to the private sector. If so, to what extent has the public sector succeeded, if not, what are the impediments? We don’t know that yet, although it is obvious that, as in any other policy implementation, there must be inherent problems that may facilitate or block risk transfer. Unfortunately, little is known in the literature. Before we investigate that claims empirically, it is important we visit the literature to examine evidence of its allocation and the views of writers and practitioners on the on-going debate over risk transfer claims.



## **1.4 Principles of Risk Transfer in PPP**

At the centre of PPP outcomes as noted is the notion of risk transfer (HM Treasury, 1995; Froud, 2003; Grahame, 2003). Risks in the context of PPP are defined as: ‘Any factor, event or influence that threatens the successful completion of a project in terms of time, costs or quality’ (EU Guidelines, 2002). The literature categories risk into design, construction, operational. Under this category of risk, the public sector spells out its output specifications and transfers the control and responsibility to the private sector to decide how to meet the pre-specified standard. Other risks are financial and demand. Financial risk refers to a future condition that cash flows might be insufficient to pay the private sector, or from supplier’s side, the private sector fails to mobilise sufficient funding for the project, and demand risk is the possibility that demand levels will not meet the expected levels needed for the private sector to recoup its investments (Grahame, 2003; Sadka, 2008). From the public sector perspective it means the possibility that the project cost will rise more than reasonably expected.

Given that each project faces a different set of risks, the UK Treasury Department, for example, laid down two principles in a framework for allocating risks between the public sector and the private sector (HM Treasury, 1995). First, project risks should be allocated to the party that is more able to manage it effectively at the lowest cost. Alternatively, where both partners have similar responsibility or control over the risk factor, the risk should be allocated to the party that is responsible or has relatively more control over the risk factor. The premise is that if the private sector, for example, is in control over those risk whilst executing the project will be motivated to select the most cost efficient process and the

resultant savings passed on to the public sector entity in the form of low contract prices (HM Treasury, 1995; Froud, 2003; Grahame, 2003) .

Based on this principle of risk allocation, project financing, delays in completion and operating risks are transferred to the private sector on the assumption that they have considerable resources and experience in managing these risks, more so than the public sector (HM Treasury, 1995; Grahame, 2003). On the other hand, risks that arise from uncertainty in the transactional environment including: (a) wrongly specified requirements, (b) catastrophic events, (c) demand and volume risks (Grahame, 2003:29) are retained by the public sector (HM Treasury, 1995; Grahame, 2003). In the case of bilateral contracting across borders, political risks, currency convertibility and transferability risks are expected to be retained by the host governments (Bayliss and Hall, 2003; Kessides, 2004). Common PPP forms and risk allocation are presented in Table 1.3.

**Table 1.3 Risk Allocations in PPP**

Responsibilities for the Public Private sectors under forms of Private Sector Participation					
Type of option	Asset Ownership	Operations and Management	Capital investment	Commercial Risk	Typical Duration
Service Contract	Public	Public and Private	Public	Public	1-2 years
Management contract	Public	Private	Public	Public	3-5 years
Lease	Public	Private	Shared	Shared	8-15 years
Concession	Public	Private	Private	Private	35-30years
Build Operate Transfer	Public and Private	Private	Private	Private	20-30years
Divestiture	Private or Public and Private	Private	Private	Private	indefinite

Source: World Bank, 1997. "Toolkits for Private Participation in Water and Sanitation.

## **1.5 Evidence of Risk Allocation to the Public Sector.**

Although the principle underlying the classification and allocation of risk is clear, there is much controversy as to whether the public sector is capable of transferring risk to the public sector. The debate arises partly because empirical studies have produced inconsistent results depending on the model used and methodology applied. A review of the PPP literature gives the impression that the public sector, especially in the UK, has succeeded in transferring risk to the private sector. Many writers (e.g. Pollock et al., 2001; Parker and Hartley, 2003;; Lonsdale, 2005a) cite a number of PPP projects, both from empirical studies and official reports, and argue that there has never been any effective risk transfer. Rather, they contend that governments continue to bear the “so called transferred risks”. In an early study, Parker and Hartley (2003) examined a UK defence contract under PPP and concluded that the intended risks were never transferred. Other studies into the NHS and IT sectors reached similar conclusions (see Grout, 1992; Pollock et al., 2001; Lonsdale, 2005b). This, it is claimed, has affected value for money for the public sector.

Staying with the UK, reports from the NAO and the Public Accounts Committee (PAC) found that some PPP projects in the health, schools and IT sectors have resulted in high cost overruns, with others re-negotiated and the original estimates revised upwards (PAC, 2003b; NAO, 2004) suggesting that private sector initiatives were costly. In all these studies, the perception running through their arguments is that the public sector incurs heavy transaction costs and, disturbingly, experience cost overruns. It is also suggested that risk, if initially transferred to the private sector, in most cases returned at the post-contractual stage.

One explanation from the literature to account for ineffective risk transfer is the difficulty in identifying and measuring appropriate risk in a particular project by public buying managers (Grout, 1997; Pollock et al., 2001, 2004; Sheil, 2002). It is argued that buying managers are incapable of identifying a priori all risks inherent in complex transactions and that what public buying managers identify as total risk are mere estimates of future events that does not reflect the actual risk (see also Grout, 1997; Hartley and Parker, 2003). It could also be argued that, given the limitation of public managers to identify risk in complex and long term projects, the problem can be compounded when it comes to identifying and measuring the non-calculable risk in a project implementation. This difficulty of identifying unexpected risk is costing the public sector more than budgeted been highlighted in a UK Treasury Taskforce report (1999/2000).

Studies revealed that at the time of signing the contract, 80% of the risks associated with the project could not be identified; they were only identified much later during the execution stage (see Pollock et al., 2001). While such an error may be considered as an innocent one, it may be symptomatic of a bigger problem concerning the identification and quantification of risk. On the other hand, the results of final cost of the projects displayed in Table 1.4 shows

**Table 1.4 PFI and Cost Overruns**

PFI/PPP Projects	Initial Cost £'million	Final Cost £'million	Percentage Increase
Norfolk and Norwich NHS Trust	90	144	60%
Greenwich Healthcare NHS Trust	35	84	140
Benefits Agency –Computers	200	1400	600%

Source: UK Treasury Taskforce 1999/2000.

clearly the tendency of the public sector to use original cost estimates in their analysis, ignoring other add-on incidental costs that occur before the project is completed. The initial project cost of £200m, NIR2 earlier touted as a PFI success story, ended up costing the UK taxpayer £1400m more than budget recording 600%.

The most significant problem the public sector faces is uncertainty. Indeed cost overruns usually experienced in PPP projects arise largely out of specification changes with the supplier which also shows the difficulty managers face when it comes to identifying future relevant risk in a relation. Even the managers are able to identify some of the risk, there is the problem of quantifying them in monetary terms and on what methodology and whose projections. These are pertinent challenges inherent in managing PPP. However, little is known. As a result, Sullivan and Ngwenyama, (2005) argue that since precise specification in hi-tech projects is impossible, and uncertainty is high, any claims that public managers are able to contract for and manage contracts for beneficial outcomes are highly contentious (see also Oxley, 1997; Lonsdale, 2005a; Zheng et al., 2008).

In a more recent NAO (2007) report, the findings showed that the UK public sector continued to experience cost overruns. Initial approved project costs of £3.704 billion for various projects for the Highways Agency increased by £1.421 billion, representing 38% overrun (NAO, 2007). Further evidence was provided by consulting firm Mott Macdonald, who were commissioned to study cost overruns in 40 large projects. The study found that cost overruns ranged from 2-24% for standard buildings, 4-51% for non-standard buildings, and up to 66% for non-standard civil engineering projects (Gaffner and Pollock, 1999; Coulson, 2008).

The issue of high transaction cost associated with PPP projects has also been challenged. In a major study into transaction costs associated with UK PPP at the procurement phase, Dudkin and Valila (2007) found evidence that the aggregate transaction costs were disproportionately higher than purported cost savings. Their study showed that the public sector often incurred an average of 10% of contract value and bidders incur 9.3% and that translates into several millions of pounds; NAO, 2003; Dudkin and Valila, 2007). They concluded that transaction cost relating to the procurement phase alone is significantly enough to wipe off any potential economic benefits of PPP. Beyond the UK, problems of risk transfer and high transaction costs have also been reported. For example, in Australia (see Wettenhall, 2003 and Sheil, 2000) and in the US (see Vining et al., 2005) studies show that PPP has not performed better for similar reasons discussed above.

From the above anecdotal evidence, it does appear that PPP or PFI arrangements are seen in some parts of the literature as not producing real benefits to the public sector. The question that arises at this point is why the public sector would like to continue to engage the public sector under PPP or PFI to operate traditional public services. This question is relevant given that many governments in developed world countries continue to implement PPP policies in public provision while those in developing countries like Ghana are being encouraged to form partnerships with the private sector. A possible explanation is that PPP arrangements may have positive values that benefit the public sector.

Indeed, some writers see the positive side of PPP demonstrated that the policy has brought about real cost savings than the inefficient traditional public procurement methods. Areas include early project completion time, technological innovation and cost savings. In an early

study of 121 selected PFI/PPP projects across the UK, NAO found from a survey that 95% of the managers of both public and private bodies believed risk had been transferred to the private sector (NAO, 2001). Writers (such as Grimsey and Lewis, 2007) have cited reports from Arthur Andersen and Enterprise LSE (2000) and the NAO (2003e) to argue that the significant improvements in the NHS, IT services, road and transportation sectors were the result of the successful transfer of risks to the private sector.

Similarly, an early HM Treasury study of seven UK PPP projects on value for money, using PSC valuations, reported an average cost saving of about 20%, amounting to about £1 billion in 2000 (HM Treasury Report, 2003a). Table 1.5 below depicts the various PFI projects data compiled by the UK Treasury showing that the UK government made cost savings in projects transferred to the private sector. From the table, total cost savings amounting to £937m were made with NIRS2 and Prime projects recording the highest yields of £195.6m and £560m respectively.

**Table 1.5 Cost Savings in PPP**

Project	Present Value of Public Sector Cost £'m	Present Value of Winning Bid £'m	Cost Savings £'m
Dartford and Gravesham	181.6	176.5	5.1
Bridgend and Fazakerley	567	513	54
4DBFOs	797	698	99
A74 ( M)/M74	210	193	17
NIRS 2	392.9	133.6	195.6
Prime	2545	1988.5	560
RAF Vehicles	24.7	18.9	5.8
TOTAL	<u>46550</u>	<u>3718.5</u>	<u>936.5</u>

Source The Treasury Taskforce 2003a

Other studies also reported PPP positive contributions in non-traditional but important areas such refuse collections. For example, Hodge (2000) found evidence of cost savings in refuse collection and cleaning services. In a similar study into PPP performance, Grimsey and Lewis (2007) provided some cases that indicated cost savings ranging between 9% and 16% IN PPP run projects. Studies by the Australian Industry Commission (1996) found cost savings ranging between 10% and 30% in private sector delivery.

In terms of timely completion of projects, The NAO (2003a) compared project cost between private financed and traditional procurement and found that 76% of the PPP projects were delivered on time and 78% within budget as compared to 30% and 27% respectively with traditional procurement. In recent times, Coulson (2008) cited the HM Treasury survey report (2006) on operational performance, which found that in 79% of projects service standards are delivered always or almost on time indicating that operational risk was passed on to the private sector.

It is clear from the above that the evidence of PPP performance relating to risk transfer and value for money is mixed and does not provide us with consistent results and explanations on the matter. It also shows that PPP analysis may turn out positive or otherwise depending on what the focus on. .

There have been several attempts to explain the cost overruns often experienced by the public sector especially in UK. It is contended that the public sector officials have the tendency to exaggerate cost savings from private funded projects in order to justify taking the public



sector down the PPP route (Gaffney and Pollocks, 1999; Sadka, 2006). In a study Sadka (2006) suggested that these exaggerations can be as high as 50% or more. He cited the Channel Tunnel project as an example, where revenues were found to have been exaggerated by two-thirds of the predicted levels (Sadka, 2006). In the UK, potential cost savings from the Dartford and Gravesham hospital project were also found to have been overstated by £12 million (NAO, 1999). Similarly, some studies report cases in which over-enthusiastic government officials in some developing countries like Argentina, Brazil, and Mexico have exaggerated cost savings in toll road projects (see Strong, Guasch and Benavidas, 2004).

A further explanation may be attributed to the methodology of calculating potential savings from PPP. The public sector comparator (PSC) is a mathematical model that uses discount rates in a finance test for PPP projects to show that the government is able to provide public infrastructure and services at lower cost than traditional public procurement (Grout, 2003; Grahame, 2003). It is often used by academics and public sector managers as a barometer to measure the level of risk transfer. The use of PSC has been criticised as an unreliable methodology because arbitrary discount rate are often used to calculate potential savings from PPP, that produce results that indicate that privately financed and managed projects are cheaper than traditional public procurement. Grout (2003) in particular found that the government has a tendency to apply 6% instead of the government standard rate of 4% discount factor for both cost of borrowing and revenues, thus producing positive savings from using private sector project financing (see also Jenkinson, 2003, p. 326).

An earlier study into the health sector by Pollock et al. (2001) has also challenged the PSC financial modelling which they considered was deliberately manipulated to provide

justification for using the private sector. The researchers further demonstrated that, had a realistic and objective discount factor been used, the private-financed initiative would have turned out to be more costly. In a separate study, Fitzgerald (2004) in Australia provided an excellent quantitative analysis to show that the discount rate used in PSC models is subjective and therefore could produce misleading results.

The other issue raised about risk transfer is the cost associated with the private sector accepting risk from the public sector. The empirical research supports the view that transferring risk and its associated uncertainty is not free but increases cost to the public sector. Given the overriding aim of the private business entity of maximising profit for shareholders, it stands to reason that risk accepted from the public sector would be valued at the going market price and passed over in the form of the contract price (Grout, 1997). As a result, the public sector is paying an unduly high price for the transfer of risks to the private sector.

In relation to above, firstly, there is a perception that suppliers deliberately put up a low bid in order to gain competitive advantage and after the contract is awarded negotiate for higher price. This view is supported by past studies, which found many UK PPP projects were priced in this way. Pollock et al. (2001) reviewed PPP in the UK health sector and found that the private sector valued risk like financing and operational risk and this is added as part of project cost. Similarly, a study by Parker and Hartley (2003) among growing cases where it has been demonstrated how risk has been passed back to the public sector (see also Shaoul, 2005; Couldson, 2008).

From the above discussions, one important issue that stands out as clear is that the public sector managers face significant uncertainty in collaborating with the private sector. It is not that public sector managers are not concerned about cost overruns, the major problem may come from the fact that managers are unable to prevent cost overruns when the private sector, after the contract has started, come back to demand price increases. Briefly, it could be argued that PPP policy is characterised with uncertainty and that gives advantage to the public sector. The review also brings to the fore the importance of the examining the economic rationale of the public sector entering into collaborative relationships, which already been shown is to transfer risk and manage uncertainty. Unfortunately, given the importance of risk transfer to the public sector this area has attracted less attention in the literature. Until now little is known about the conditions that influences risk transfer. This is significant because, as the review has shown, the public sector is said to achieve good value for money when the appropriate risk is transferred to the private sector. Moreover, little is known about the methodology by which risk in a relationship is shared between a buyer and a supplier. Although there has been some attempts to show that risk transfer requires genuine alignment of interest with the private sector (see Cox et al., 2004; Lonsdale, 2005a) much is yet to be known about conditions that create genuine alignment of interest between a buyer and a supplier. Given the importance of balance in PPP, it would seem the issue of balance would have been given much more scholarly attention than it is receiving. Those studies that explored the issue of symmetry between the public sector and the private seeking to unravel the mystery of risk transfer are mostly illustrative and descriptive and does not delve deeper into the problem therefore offer little guidance as to the various impediments to the development of balance. This, at least in part, originates from the fact that most researchers focus on successful cases using TCE analysis as a result failed to investigate properly problems that confront the public sector in their efforts to transfer risk to the private sector.

Therefore, it is important to examine the impediments to the balance in PPP. This brings to the fore the importance the core question of whether PPP in its present state could be described as an inter-dependent one that fosters the sharing of risk in a mutual satisfaction way. Since the focus of the study is to investigate whether the public sector has the ability to develop a balance with the private sector so as to transfer risk to the private sector, it is important we discuss the definition of PPP which is taken in the next section before we proceed further with our study.

## **1.6 PPP Definition**

### **1.6.1 Introduction**

One aspect that has not been provided yet in this chapter is a definition of the term PPP. As can be seen from the above, PPP is a broad concept used in the public management literature to describe a wide range of ‘partnership’ relationships that can be developed, from not-for-profit voluntary partnerships to legally-binding commercial ones. The preceding literature review took the usage of the term PPP by the various participants in the literature at face value. This was purposely done in order not to exclude large parts of ‘PPP’ literature, which would have happened if a definition had been established upfront. At this stage, however, it is important to develop a working definition of PPP, within the context of the study. To do this, the author reviews various attempts made to define PPP and then justifies his own.

In this section, we examine the definition of partnership and how different scholars have conceptualised it within PPP. The author attempts to bring them together to increase our understanding of what constitutes its essence. Finally, we develop the working definition

from the concepts and ideas of Williamson. This is deemed appropriate for further analytical research on PPP in this thesis. The objective is to drive the research by advancing a theoretical framework that identifies a number of variables that help to promote or hinder the developing of a state of partnership that satisfies both parties.

### **1.6.2 PPP Definition**

In recent years, studies on PPP have recognised it as essential for increased economic activity and competitiveness. Yet there is still no consensus among researchers on how PPP should be defined. The PPP concept is subjected to different interpretation and definitions, at different levels in different contexts with different objectives (Geddes, 2005). Partnerships can be voluntary or for commercial purposes. In public-private sector business arrangements, PPP can take many forms, ranging from Build Operate and Transfer (BOT) to service contracts, from multi-million dollar global projects to low budget community-based projects. Partnerships can be bilateral or multilateral bodies and actors can include local or multi-national private businesses, non-governmental bodies or policy think tanks (Steets and Thomsen, 2009). PPP can also be viewed as horizontal or vertical (Geddes, 2005).

Due to its diversity in dimension and purpose, various writers and policy makers have defined PPP in various ways, some loosely, others in a specific context, illustrating the fact that the term PPP is not understood universally. Indeed, the literature acknowledges that PPP definition has always been a challenge (Wettenhall, 2003; Geddes, 2005; Lonsdale, 2007; Schaffhaff and Kaan, 2007) and a matter of contention (Schaffhaff and Kaan, 2007). This

conceptual difficulty is complicated further by the temptation of many government officials to confuse PPP with privatisation.

In PPP, public sector bodies and private sector entities retain control, but are expected to share costs, rewards, and responsibilities. On the other hand, privatisation represents the transfer of control and ownership risks and rewards to the private sector. Confusion like this appears to impede rational discussions about PPP, since all the negative inferences of privatisation are applied to PPPs as well (Schaffhaff and Kaan, 2007).

The Oxford Dictionary (2002) defines a 'partnership' as a 'joint business with shared risks and profits'. Nelson's definition is similar but he added words like 'shared responsibilities' (Nelson 2002:46). Beyond the literal meaning of partnership, a review of the literature shows that PPP definitions have been approached from different perspectives and have been associated with a number of strategic and operational perspectives (Wettenhall, 2003; Geddes, 2005:p.114).

Strategically, partnerships are defined as purposive relationships between independent firms who share compatible goals, strive for mutual benefits, and acknowledge a high level of mutual interdependence. From this conceptual view, partnerships are formed for the purpose of achieving goals and benefits that individual firms could not attain easily. For example, some writers (Klijn, 1996; Bigelow, 2001; Nickerson and Silverman, 2003; Allen and Philips, 2003) conceptualise partnership as interdependent and co-equal and argue that partnership connotes an intention to create symmetry of the partners' interests and objectives. From this

conceptual view, partnership emerges as a state of natural equality. Features include partners' readiness to demonstrate tolerance, the adoption of flexibility in decision-making, openness to diverse experiences and commitments to each other's goals.

Others see partnership in the public sector as political, concerning policy formulation. Thus from a political perspective, PPP is conceived as a policy tool for achieving governmental objectives without directly getting involved in risky decisions and changes. For example, Bult-Spiering and Dewulf (2006) defined partnership as a political tool that allows public bureaucrats to use the private sector to achieve governmental programmes and objectives see also Froud, 2003). Similarly, Hess and Adams (2001) identify partnership as an emerging policy tool for tapping into the discipline of the market.

PPP has been conceptualised as a joint venture in which public and private sector bodies pull their resources and expertise together to support a government's infrastructure development programme in specific areas in the economy (Pollock et al., 2001, p275). Carroll and Steane (2000), for example, broadly defined PPP as 'agreed, co-operative ventures that involve at least one public and one private sector institution as partners' The writers further described PPP along the lines of partnership as an arrangement that allows a public sector body to engage a private company to achieve developmental objectives set by the political authorities. The Canadian Council appeared to favour this view when it defined PPP as a venture 'between the public and private sectors built on expertise of each other that best meets clearly defined public needs through the appropriate allocation of resources, risks and rewards' (Canadian Council, 2003).

Operationally, PPP can be defined in terms of relationship management and the setting of goals and outcomes. This includes setting up flexible arrangements under terms where both parties have confidence to work together to create value for themselves. For Macneil (1978) PPP is said to bring about operational efficiency resulting in beneficial outcomes to both parties under the so-called ‘win-win’ philosophical underpinnings.

Some writers also define PPP as project orientated activities, similar to the classical contracting model. Blanc-Blude et al. (2007) define PPP to include the design, construction, operation and maintenance of a facility with major components of private finance. The more common operational labels such as co-ordination, collaboration, and joint steering committees are used to indicate evidence of a PPP arrangement (see Huxham, 1996; Glendinning, 2003).

Alternatively, other writers focus on the input and output of resources or outcomes that partners are expected to produce. Those who approach PPP definition from an input/output perspective describe it in terms of purposes, structures and operating procedures between the public and private bodies for a pre-defined objective of the public sector body (Huxham, 1996; Warner and Hebdon, 2001; Nelson, 2002; Wettenhall, 2003). From this conceptual view, the public sector defines the standard of service which the private sector is expected to execute, and performance is measured along these benchmarks. The IMF, the World Bank and other multi-lateral partners’ output measures appear to fall within this category, laying emphasis on private sector output (Tiong, 1990; Middleton, 2000; World Bank, 2004b).



Indeed, the World Bank definition of PPP is illustrative. The Bank defines PPP as the ‘combination of a public needs with private capability and resources to create a market opportunity through which the public need is met and a profit is made’ (World Bank, 2004b). In this definition, a problem of partnership emerges which has to do with the contrast between the two different agendas of the two parties. Whilst the public sector defines partnership in terms of achieving good value for money, the supplier side considers it as a commercial opportunity to make profits (Bartley, 1996, p731).

In recent times, PPP has become synonymous with the loose idea that PPP is about the transfer of risks to the private sector. The Institute for Public Policy Research (IPPR) described partnership as ‘a risk-sharing relationship, based upon a shared aspiration between the public sector and one or more partners from the private and/or voluntary sectors to deliver a publicly agreed outcome and for public service’ (Geddes, 2005, p.40). A similar definition from the Commission on Public Private Partnership (2001) considered partnership as a mechanism for sharing risks between the demand side, i.e. the government, as a buyer, and the supply side.

Similar to the above, the Organisation for Economic Co-operation and Development (OECD) focuses on the alignment of public and private sector objectives. For example, OECD defined PPP as a partnership “between the government and one or more private partners, according to which the private partners deliver a public service in such a manner that the service delivery objectives of the government are aligned with the profit objectives of the private partners” (OECD, 2008). However, the definition added that the effectiveness of the alignment depends

on sufficient transfer of risk to the private partners, a proposition that runs through many of the definitions earlier reviewed.

All the above conceptual view of partnership provides us with clear indication that scholars, practitioners and funding agencies perceive PPP role as risk transfer and its management- it is a controversial issue where there is intense debate has received less research attention on the constraints to successful risk transfer. Although, these definitions remain important in the literature it is essential that we subject these risk transfer claims to strict empirical analysis. To this end the above definitions are either too broad or descriptive. Furthermore, defining partnership in terms of risk and reward sharing within a philosophy of equality is also too vague to be of any analytical value in allowing us to operationalise partnership for measurement. As a result, it is necessary for the author to move away from the definitions provided by participants in the PPP policy arena towards guidance provided by the economics literature (Lonsdale, 2005b). The reason is that, since 1983, economics literature has moved away from a simple adherence to traditional neo-classical models to more 'realist' ones that reflect the practical business world of bilateral contracting. Attention would be focused on two strands of the literature, on property rights and Transaction Cost Economics (TCE) theory, from which the researcher teases out the working definition for this study.

In the property rights literature, as developed by Grossman and Hart (1986) and Hart and More (1990), the incentive effects of asset ownership imply that shared ownership of economic producing assets maximises joint gains and minimises acts that will put their investments at risk. This implies that in PPP, both the public sector and private sector adopt at

the outset an efficient ownership and control governance structures to share risks and gains efficiently (see Engel et al., 2008). In this way, joint interest in the relation creates bonding.

Although this is found to be an improvement in the attempt to define PPP it is analytically problematic, as the definition ignores the relationship between partners' interests and resources that may not be commensurate in value distribution or the effect of bargaining power over divisions of relationship surplus or the residual control rights of non-human assets.

We now turn to the more comprehensive definition of PPP obtained from the Transaction Cost Economics (TCE) literature, initially developed by Williamson (1975). TCE conceptualises 'partnership' as a bilateral contracting arrangement that seeks to promote interdependent business relations between economic actors. In defining bilateral governance, TCE takes a balance, a stance, in respect of the need to manage the risks arising from asset specific investments. Williamson shows that bilateral contracting allows both the public and the private sectors to jointly invest in transaction specific assets to reap the gains from trade for mutual benefit (Williamson, 1991).

In relation to the breakdown of classical contracting under conditions of asset specificity and uncertainty, Williamson gave the rationale for bilateral contracting: 'Individuals who are responsible for adapting interfaces have personal as well as an organisation stake in what transpires' (Williamson, 1996, p. 104). Williamson further explained that 'individuals located at the interfaces may refuse to be part of opportunistic effects to take advantage of (rely on)

the letter of the contract when the spirit of the exchange is emasculated.’ This implies that wealth creation constraints are assumed away and the prediction is that parties in partnership are willing and able to collaborate with each other to create interdependent relations (Hart and Moore, 1990; Williamson, 1996).

In summary, this chapter has discussed the importance of PPP and noted its benefits; drivers noted the importance of risk transfer in the management of PPP. We also discussed the debate on risk transfer to the private sector and cost minimisation. Whilst various studies point to examples of PPP that have effectively transferred risks to the private sector, others provide a different picture that indicates fairly ineffective risk transfer and high project cost overruns. The inconsistencies in the managing risk transfer ignited PPP debate and provided the impetus for us to seek empirical evidence as a way to enrich our understanding of the phenomenon. This led us to examine the definition of PPP from different perspectives to help us contextualise and develop a working definition for our research using Ghana as a research focus. We found among other things that PPP is all about risk transfer but that also leaves us with contestable implied assumption of balance under TCE theory.

As has been developed from the literature, TCE assumes an equilibrium state in which the current and future states, action, or decisions of partners are committed to create mutuality for efficient outcomes. Given that this issue of a balance is central to the thesis, the author now proceeds to examine TCE literature and other perspectives of agency theory and property rights theory as they relates to bilateral governance and deal with the issues raised in the subsequent chapters.

## **CHAPTER 2**

### **Literature Overview of Bilateral Governance**

#### **2.1 Introduction**

In the previous chapter, we defined PPP in terms of the TCE mechanism of bilateral contracting. Underpinning this definition is the TCE assumption that bilateral governance allows parties to manage their uncertainty through collaboration. In addition, bilateral governance provides buyers with the basis for safely negotiating the variations that arise out of transactional uncertainty. However, others are less optimistic about balance in bilateral governance and worry about the TCE solution to lock-in problems that characterises all forms of bilateral contracting.

This debate over balance is central to this thesis. Not only does PPP resemble the bilateral contracting mechanism put forward by TCE (in its use as a definition), but the policy statements of many governments and TNOs, such as the World Bank, also take the TCE view, or at least invest in the hope that such mechanisms can be balanced in the manner of TCE. Yet a potential problem of PPP is the ability of contractual authorities to get the right balance, deemed important because it facilitates the transfer of risk over the life of the contract relation. This chapter looks at the issue of post-contractual balance in more detail. In this chapter we discuss the contribution that TCE can make to efficient management of PPP contracts between the public sector and the private sector. We also draw together other

incentive theories of agency and property rights that focus on how autonomous economic agents design efficient contracts in a way to prevent or minimise risk in business exchanges.

The chapter is organised as follows: Section 2.2 discusses generally the principal agency theory and property rights theory followed by the rationale for the choice of TCE theory for this study. Section 2.3 introduces the TCE theory used in this study. This is followed by discussions on the interplay of opportunism, bounded rationality, asset specificity and uncertainty and the use of credible commitments. Section 2.5 discusses bilateral governance and section. Section 2.6 discusses the TCE's confidence that buying managers have the ability to balance their relation through shared investments or financial hostages. This is followed by concluding comments that introduces the critique of TCE assumptions on bilateral governance balance.

## **2.2 Models of Contract Management**

In contract management literature, there are basically three broad theories of incentive contracting in economics: agency theory, property rights theory (PRT) and TCE (Mahoney 1990; Alchian and Demsetz, 1972; Brousseau and Glachant, 2002) These theories individually provide guidance to autonomous actors on how to design efficient contractual solutions to protect themselves economic against problem of risk. Brousseau and Glachant (2002) noted that these three schools of thought in economics of contracting dominate the field of incentive contracting in economics. Given that PPP is affected by the economics of contracting, each of the models will be briefly discussed before focusing on TCE theory to investigate whether the Ghanaian public sector may or may not be able to develop post-contractual balance as prescribed. We take a look at agency theory first followed by property rights theory.

### **2.2.1 Agency Theory**

The agency theory approach to contract management is widely used by scholars to describe the contractual relationship when one party (the principal) engages another party (i.e. the agent) to act on its behalf. According to (Jensen and Meckling (1976, p. 5), an agency relationship: is created when 'one or more persons (the principals) engage another person (the agent) to take actions on behalf of the principals that involve the delegation of some decision-making authority to the agent.

The theory assumes that principals and agents have different agendas and attitudes towards risk sharing (goal conflict). This goal conflict may, in turn result in one or both parties undertake actions that may be against the interest of the other party (Jensen and Meckling, 1976; Holmstrom, 1979). Agency framework provides that unless the agent's behaviour is controlled through incentive contracts, conflict of interests is likely to arise to undermine the interests of the principal (Kotovitz, 1987; Jensen and Meckling, 1976).

The agency model recognises two broad strategic behaviours as adverse selection and moral hazards (Akerlof, 1970; Jensen and Meckling, 1976; Mahoney, 1990). An adverse-selection is an ex-ante strategic behaviour problem and it appears when the agent withholds private information about its own capabilities from the principal or the principal made a wrong choice of selecting an agent as result of lack of information on agent's actual capacity to deliver as expected (Akerlof, 1970: Jensen and Meckling, 1976).

A moral hazard, on the other hand, is an ex post-contractual strategic behaviour and it arises when the principal cannot observe the agent's actions either because the agent is more expert in their task or monitoring costs are found to be prohibitively higher than the savings to be

made by doing so. Both adverse selection and moral hazards may explain why a principal may not achieve functionality and cost efficiency from agency relationships (Jensen and Meckling, 1976).

The major contribution of agency theory to efficient contract design is that it points out the possibility of goal conflict of the agent and moral hazards as a result of information asymmetry. Thus the agency model focuses on the need for the principal to craft risk-incentive mechanism into the contract design in a way that the motivational goals of the agent are aligned with his interests.

However, the agency model has some weaknesses. Perrow (1986) and others have criticised agency theory for ignoring complex issues of competition and lack testable hypothesis. The agency model has also been criticised for assuming that ex post bargaining is efficient and ex ante incentive alignment for specified incentives could easily lead to predictable outcomes. This assumption is argued to ignore the possibility that increasing uncertainty makes it expensive to shift risk despite the motivational benefits to do so (Perrow, 1986; Eisenhardt, 1989). Williamson (1983) commented on the weakness of the agency model of assuming zero cost transaction and noted that output measures such as functionality and quality cannot be measured in reasonable accuracy a priori. Agency model also Brousseau and Glachant (2002) noted that the agency model ignores property rights.



### **2.2.2 Property Rights Model**

The PRT on the other hand focuses on the assignment of rights to owners of economic assets (Coase, 1960). Property rights theory hold that economic activities include exchange of resources that can be bundled into property rights (Demsetz, 1964; Alchian and Demsetz 1972). In the economics literature property rights refer to the rights to use, right to earn income from, and to transfer or exchange to assets and resources. The distribution of income generated by collected effort by different contracting parties pursuing different agenda motives leads to inefficient positioning and therefore carries some forms of risk and cost. The main arguments in the PRT theory is that unless the investing party is given the control and residual rights over his assets, they may be exposed to the hazards of hold-up and opportunism (Holmstrom and Milgrom, 1979, 1994; Demsetz, 1964). In effect, property rights specification arise in response to the economic problem of allocating scarce resources, and the assigning of property rights affects economic behaviour and economic outcomes (Coase, 1960; Demsetz, 1964).

The major contribution of PRT to contract design is the modelling of ownership and incentive structures put forward by Grossman and Hart, (1986) and Hart and Moore (1990). The model prescribes that the owner of the assets should be given the right to take decisions and in extreme cases where uncertainty is high should adopt joint sharing of the risk in the assets. Perhaps, the most important contribution PRT theories to contract management are in the area of supporting economic activities through legal protection (Libecap, 1989). For example, countries with effective property rights regime have been able to attract investors because investor's assets are safe (North 1990; Olson, 2000; Woodhouse E. J, (2008).

Like the agency model, the PRT model suffers from some weaknesses. Williamson (2002) commented on the problem of property rights by arguing that given the pervasive information, uncertainty and complexity that affects property rights it is not feasible to bargain efficiently at the beginning of the contract. In other words, PRT ignores the cost involved in trying to specify ways to respond to changes in the environment and enforcements (Demsetz, 1998; Brousseau and Glachant, 2002). Moreover, some writers, such as North (1990) and Williamson, 2002) commented that it is difficult to operationalise the important explanatory elements in property rights models.

The third, approach to incentive contract design is TCE. As it would be discussed in greater detail in the chapter, TCE offers a different perspective to what constitutes contractual problems and the corresponding solutions for them. Notwithstanding, their obvious differences in their assumptions on contractual efficiency, are useful in providing important understanding of various contracting problems both in the private business sector and in the public sector.

### **2.2.3 Justification of TCE**

This study adopts TCE as the dominant theory to investigate the causes and problem of hold-ups in the telecoms and water contracts. While it cannot be denied that agency theory and PRT can explain opportunistic behaviour through the contractual incentives framework, neither of them would be helpful to answer the research question. In particular, the research question is formulated around TCE assumption and that makes TCE as obvious theory to focus on, even though agency and PRT theories may be found useful to the study. TCE

reasoning has serious implications for public policy. Reviews undertaken by Macher and Richman (2006), for example, on TCE show that it has relevance as a guide to public policy and practice and had been used in number of management studies (see also Joskow, 1988; 1990; Saussier, 2004).

## **2.3 Overview of TCE Theory**

In Chapter One, we noted that PPP policy has generated debate on the key criteria of risk transfer and high cost overruns to the public sector at a time when the PPP approach to public sector procurement is growing in influence and practice worldwide. As was noted, many writers continued to be sceptical about the arguments in support of private sector participation in public provision principally because of possible contractual failures and high cost overruns. However, the problem of PPP contracting is better explained through economic theory on transaction costs analysis, as espoused by Williamson.

TCE is a branch of organisational economics that focuses mainly on firms, markets, and other forms of contracting and seen as governance structures to minimise transaction costs and to achieve efficient outcomes (Williamson, 1985). Williamson, drawing from Coase's (1937) ideas, posits that the main purpose of economic institutions of capitalism is economising on transaction costs during exchanges with third parties (Williamson, 1985). In this context organisations are viewed as collections of explicit or implicit contracts characterised by incomplete specification of contingencies and therefore involve transaction costs. Williamson distinguishes transaction costs from production costs and defines transaction costs as those

incurred in every transaction when ‘a good or service is transferred across a technologically separable interface. One stage of activity is terminated and another begins’ (Williamson, 1981, p. 552; 1996a, p. 58). Some writers have provided their own definitions. Arrow defines transaction costs as the ‘costs of running the economic system’ (Arrow 1969, p. 48) and argues that its identification in different contracts and under different systems of resource allocation is important. Dahlman (1979) distinguishes three categories of transaction costs: search for information costs, bargaining and decision costs and enforcement costs. Combining Williamson’s definition and that of Arrow and others, the picture that emerges is that transaction costs arise every time business exchanges take place with a third party. These costs include the costs of selection and negotiating monitoring and enforcing contractual obligations.<sup>3</sup>

In TCE analysis, the methodology for economising these costs ‘entails an examination of the comparative costs of planning, adapting, and monitoring task completion under alternative governance’ studies (Williamson, 1996a, p. 58). This implies that managers consider possibilities of how to organise a transaction at relative cost. According to Williamson, managers may choose market transaction or organise it in-house. The other form of governance that had emerged between the continuum between markets and in house is the hybrid form of governance. PPP falls under the hybrid governance and is further discussed later in the chapter. Table 2.1 shows the various types of governance structures. Each of these modes of governance is supported by specialised institutional structures in which ‘the integrity of a transaction or related set of transactions is decided’ (Williamson, 1996, p. 11). Detailed discussion on the dichotomy between market and internal provision (hierarchies) are

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<sup>3</sup> The relevance of transaction costs as they relate to contract management is that they cause economic friction and this is distinguished from production costs.

beyond this thesis even though its significance cannot be lost on the hybrid form this thesis is interested in.

**Table 2.1 Transaction Characteristics and Governance Structure**

		Investment Characteristics		
		Nonspecific	Mixed	Idiosyncratic
Frequency	Occasional	Market Governance (Classical Contracting)	Trilateral Governance (Neoclassical Contracting)	Governance Contracting
	Recurrent		Bilateral Governance (Relational Contracting)	Unified Governance Contracting

Matching governance structures and Attributes of Transactions. (Source Williamson, 1979)

In general terms, although the market enjoys the advantage of being able to use competition to fix optimal prices, this advantage is shifted to the internal provision when a transaction requires special need for future adaptation and re-negotiations (Williamson, 1975, 2008). The reason is that market transactions contain frictions that could lead to ‘market failure’, particularly when firms attempt to enter into long-term business collaboration to buy or sell goods and services supported by specialised assets. These market failures, in the TCE view, are bounded rationality opportunism, asset specificity and uncertainty (Williamson, 1985). Crucially, it could be demonstrated that the above variables are also contractual problems in PPP at least, from TCE perspectives. As a result, it is important we understand their theoretical implications and contractual solutions proposed by Williamson to design them away efficiently in a contract design (Mahoney, 1990).<sup>4</sup>. In the next section, we discuss briefly his behavioural assumptions and transactional characteristics.

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<sup>4</sup> Managers are therefore called to organise transactions so as to ‘economise on bounded rationality while simultaneously safeguarding themselves against the hazards of opportunism’ (Williamson, 1985).

### **2.3.1 Behavioural Assumptions**

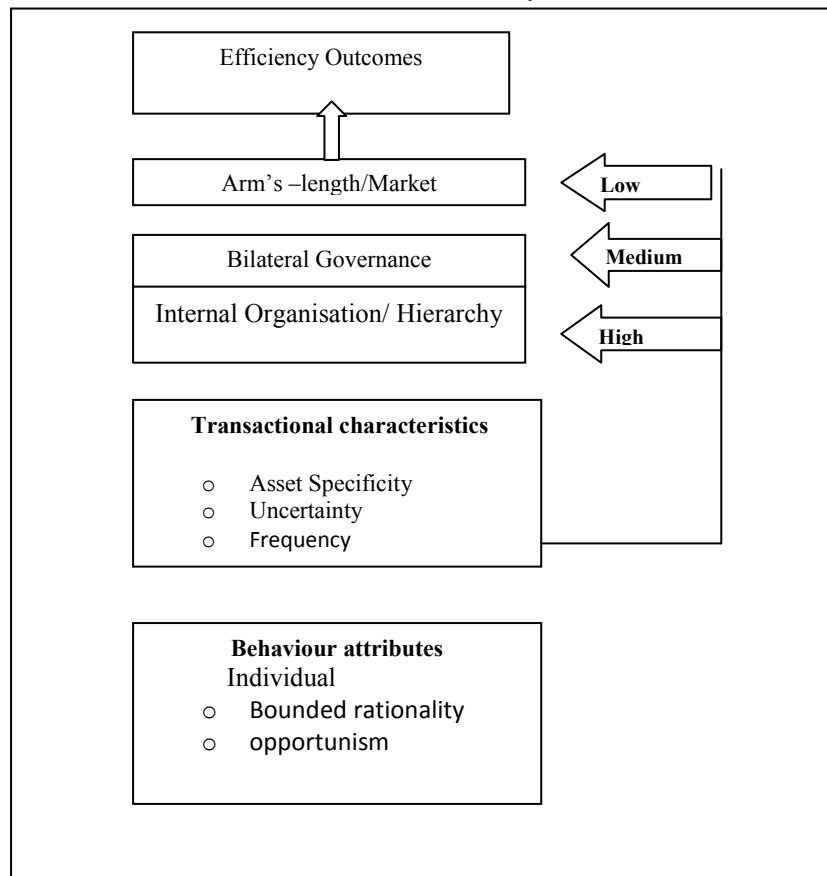
TCE is one of a number of schools of thought that has made the issue of human behaviour a central element in theoretical discussions of economic organisations. Other behavioural economics and trust-based schools too have highlighted the importance of human nature in inter-firm relations (for example, Simon, 1957; Levinthal and March, 1993; Bromiley and Flemming, 2002). Simon (1957; 1955), for example, in relation to efficiency outcomes, urges that the study of human behaviour should form the basis of a research agenda.

Following Simon (1957) and drawing much of his material from the behavioural economics literature, Williamson (1975) developed two behavioural concepts into his analytical framework and insisted that the study of human behaviour is critical to an understanding of how economic actors think and how their minds work (Williamson, 1979). He identified two human traits - the conditions of cognition and self-interest orientation- and described them as problematic in contract management. He summarised his rationale for placing human behavioural assumptions at the height of his analysis as that ‘human imagination and ability to surprise opponents is high and that knowledge of particulars, moreover, does not preclude surprises.’

In support of his assumptions, Williamson, citing Simon (1985, p. 302) said: ‘Nothing is more fundamental in setting our research agenda and informing our research methods than our view of the nature of the human beings whose behaviour we are studying’, making reference to cognitive and self-interestedness of humans. This may also implies that the study of contractual problems also requires the understanding of human motivation in business

relations (Williamson, 1985. p. 58). It is with this in mind that we examine TCE behavioural assumptions of TCE. The framework for transaction cost analysis is depicted in Figure 2.1

**Figure 2.1 Framework for Transaction Cost Analysis**



In what follows, therefore, bounded rationality and opportunism will be discussed in detail. Later in the discussion, the third behavioural assumption will be discussed: human foresight that allows decision makers to partially overcome their cognitive limitations.

### **2.3.1.1 Bounded Rationality**

Economists have long worked on the assumption that humans conform to the model of rational utility maximisation (Simon, 1955; March, 1994). Under the rational model, decision makers are assumed to be perfect calculating machines, able to predict accurately from the costless information in the environment (Simon, 1955). The rational model has the following assumptions:

- (a) humans have access to relevant information
- (b) there are no limits on the extent of information gathering
- (c) information is available to humans at no cost

Williamson, amongst others, has challenged this assumption (see also Edgeworth, 1890; Hall and Hitch, 1939). For example, Edgeworth described humans as having ‘limited intelligence’ (1890:467), and Almond (1945) used ‘limited rationality’ to describe human limitations in making informed decisions. Simon (1955: 1957), on his part, pioneered a paradigm shift from the more optimistic neoclassical view of man as a rational being to a more cautious one of near rationality. His justification was that there are limits on the ability of actors to search for and process information (Simon, 1955).

Relying on Simon and others from the behavioural school, Williamson defined bounded rationality as a behaviour that is ‘intendedly rational, but limitedly only so’ and argued that economic actors would not be able to write a complete contract (Williamson, 1996, P. 6). The



literature offers a number of reasons why economic agents would not be able to write a complete contract, of which the condition of bounded rationality is part.

The TCE literature offers a number of reasons why economic agents would not be able to write a complete contract, of which the condition of bounded rationality is part. First, cognitive limitations mean that it is not possible for agents to assemble all necessary information, thus contracts will always be incomplete with errors, gaps, and omissions. Even where complete information is available, it is contended, it may be a costly exercise to write all of them in one document for third party enforcements by the courts (see Milgrom and Roberts, 1992; Williamson, 1996). The central message is that economic actors are rationally bounded in one or the other and that create risk in business exchanges. However, bounded rationality on its own does not tell us anything about why contracts fail or increases cost of doing business with third parties. This takes us to the second assumption of opportunism in the TCE framework. The next section discusses the second behavioural assumption of opportunism which in the presence of bounded rationality creates problems in business exchanges.

### **2.3.1.2 Opportunism**

The second behavioural assumption in the TCE framework is opportunism. A major objective of individuals in economic exchange is the self-interest to maximise their interests. However, self-interests may move beyond normal pursuit of one's interests to where cheating and deception are employed as strategic behaviour to maximise their profitability at the expense of the other party in an exchange. Williamson defined opportunism simply as 'self-interest

seeking with guile' (Williamson 1975:6: 1985 p. 47). He used the word 'guile' to differential simple self-interest from dishonest acts to include 'calculated efforts to mislead, distort, disguise, obfuscate, or otherwise confuse,' Williamson (1985) assumed that economic agents have the propensity to cheat given the opportunity to maximise their interests. However, further contributions to the concept of opportunism have identified that opportunism may be explicit or subtle and therefore difficult to detect. For example, the literature identifies acts such as refusing to honour contractual terms, walking away from contracts or other deliberate acts with an intention to cheat are all explicit form of opportunism (Williamson, 1985; 1996; Wathne and Heide, 2000). For example, Muris (1981, p. 521), agreeing with that definition of opportunism, added that opportunism occurs when a party behaves, contrary to the understanding of the contract, but not necessarily contrary to the agreement's explicit terms, resulting to a transfer of wealth from the other party to the performer.

Subtle opportunism, on the other hand, can take the form of withholding information or making false representations during negotiations similar to adverse selection or moral hazards in agency relationships. Examples of subtle opportunistic acts that may lack visibility to a contracting party include quality shading and the withholding of effort or shirking (moral hazards) which is consistent with agency framework. The other important aspect of opportunism pointed out in the literature is the distinction made between opportunistic attitude and opportunistic behaviour. Williamson (1975, p. 48) refers to opportunistic attitudes as one of the 'rudimentary attributes of human nature,' implying that this particular human attitude is relatively stable and unaffected by a given situation. In contrast, opportunistic behaviour could be dictated by incentives that are present in a given situation that may encourage or deter opportunistic behaviours (Williamson, 1975). Opportunistic behaviour can be interpreted as one that may be triggered in many situations when gains from

short-term opportunistic acts are attractive or where the possibility of detection is low (see Williamson 1975; 1985). This is the real threat in business exchanges as inaccurate information about the intention of a potential supplier is the source of transaction cost. This part of new meaning to opportunism as a pervasive human failing is not only controversial but has generated a lot of debate in the literature. The basis of the debate will be made clearer as we review TCE literature.

### 2.3.1.3 The Significance of the Behavioural Assumptions

The TCE literature uses the behavioural assumptions to explain the complex problems in economic exchange and their significance on efficient outcomes. The effect of both bounded rationality and opportunism on market exchanges is illustrated in a matrix in Figure 2.2 below.

**Figure 2.2 Contracting in the Context of Bounded Rationality and Oppottunism**

		Contract Management (TCE Approach)	
<b>Condition of Opportunism</b>	Absent	[A] Bliss	[C] General Clause Contracting
	Present	[B] Comprehensive Contracting	[D] Serious Contracting Difficulties
		Absence	Present
		<b>Conditions of Bounded Rationality</b>	

Source: Williamson, Oliver E. (1985) *The Economic Institutions of Capitalism*, New York, Free Press (p. 67)

The matrix consists of four different types of marketing conditions which correspond to bounded rationality and opportunism. The model specifies four distinct contracting conditions an economic actor is likely to be located. In cell (A), the key information about the transaction is available to each party and there is no opportunism. This is the ideal market for economic actors to engage in economic activity to achieve efficiency. However in real life, this condition hardly occurs. The other cells B, C, and D, present us with the practical problem when one, or both bounded rationality of opportunism is present. If a transaction takes place under a condition of unbounded rationality and presence of opportunism, the likelihood of opportunism occurring can be foreseen, and, as a precaution, extra-safeguards can be crafted in the contract design to deal comprehensively with the risk. This form of comprehensive contracting is in cell (B). Similarly, where opportunism is absent, but limited information is present, parties are able to respond to contractual problems that may occur in the course of the exchange. This type of contracting takes place in cell (c) and is where relational contracting is developed (see McNeil, 1978, Granovetter, 1985). However, where both parties are rationally bounded but opportunism is present are present in a given transaction, then both parties face the most difficult contracting environment and, as a consequence, lead to market failures. Unfortunately, TCE argues that this is where most economic exchanges take place under the conditions described in cell (d). Interestingly, bilateral contracting, the focus of this thesis, is also located here.

Going by Williamson's model of contracting claims, one is tempted to regard opportunism as pervasive in economic exchanges and that together with bounded rationality buyer-supplier exchanges may not be efficient. Williamson appears to hold that view strongly when he

contended that contractual difficulties ‘would vanish were it not for the twin conditions of bounded rationality and opportunism’ (Williamson, 1996a, p. 10).

However, the debates over the centrality of opportunism in transaction cost analysis shows that not everybody shares that view (see Alchian and Woodward, 1988; Coase; 1991). For example, Coase reject the idea that opportunism is an important factor in business relationships nor does he accept the idea that asset specificity exposes a firm to opportunism and therefore lead to integration. For example, Coase (1991, p, 71-72), made reference to Smith contract with GM and argued that there was a harmonious relationship between the two and that GM did not resort to post-contractual opportunism despite much of the dedicated machinery was specific to GM.

The debate over opportunism is irrelevant to our present study. What is important, though from the debate what that means to the public sector manager in managing PPP. On the other hand, as opportunism debate continues PPP empirical studies in UK, USA, and Australia provide the evidence that opportunism remains the major cause of high transaction costs. However, it is unclear where the dividing line should be drawn between potential opportunist suppliers and those who are not given public sector is interested in post-contractual protection against risk of opportunism. Before we look into the various mechanisms available to managers to design efficient contract to achieve optimal supplier performance, we shift our attention to the second block in the TCE framework related to transaction characteristics of asset specificity, uncertainty and frequency.

### **2.3 .1.4 Transactional Characteristics**

The previous section discussed the behavioural assumptions that underpin the TCE analysis. In this section, we focus on the three attributes of a transaction identified as asset specificity, uncertainty and frequency. The objective here is to examine how these transaction attributes interact with bounded rationality and opportunism to create contractual problem impediments to efficient contract design. TCE identifies the attributes of a transaction -asset specificity, uncertainty and frequency as central to its hypothesis. Their full implications for the post-contractual hold-up will be discussed in the following section.

One of the problems faced by early transaction cost theorists was how to make transaction costs operational. This problem was solved when Williamson made the characteristics of a transaction the unit of analysis in his framework focusing on the main analytical properties of a transaction (Williamson, 1975; 1996). Williamson argued that taking the transaction as the basic unit of analysis allows transaction costs to be operationalised in line with the three conditions proposed earlier by Commons (1932) solves the methodological problem in analysis contractual relationships. According to the guidelines laid down by Commons (1932), any unit of analysis should contain ‘in itself the three principles of conflict, mutuality, and order’ (Commons 1932, p. 4). Williamson (1975; 1996) further noted that the degree of each attribute in each particular transaction can be measured reasonably and this allows the theory to focus primarily on micro-analytical questions (for example, the comparative efficacy with alternative generic forms of governance, market, hierarchies and hybrids to economise on transaction costs. TCE identified the attributes of a transaction -asset specificity, uncertainty

and frequency as central to its hypothesis. Their full implications for the post-contractual hold-up are discussed below.

Asset specificity: Asset specificity is perhaps the most important transaction characteristic in TCE framework. Williamson (1985) defines asset specificity as ‘durable investments that are undertaken in support of a particular transaction, the opportunity cost of which investment is much lower in best alternative uses or by alternative users should the original transaction be terminated.’ These transaction dedicated assets cover physical, human resources and intangibles.

Specifically, the literature distinguishes six primary types of asset specificity: (1) site specificity, where businesses are located together to economise on inventory and transportation expenses; (2) physical asset specificity related to the plant, machinery or tools needed to carry out specific tasks (3) dedicated assets, which are discrete investments in general purpose plants that are made purposely to suit a particular customer; (4) ‘brand name capital’ and (5) temporal specificity in investments to support timely on-site responsiveness (6) dedicated assets specially developed to serve the special needs of a large customer (Williamson, 1991,1996).

In recent times, non-physical human asset specificity related to specialised knowledge such as research and development and firm-specific knowledge have come under asset specificity. Mortensen (1978) suggested that human specificity involves the experience and skills required in training some workers (e.g. Poppo and Zenger, 1998) have suggested that shared

language, knowledge and routines should be considered as asset specificity in partnerships, arguing that their value is limited to that relationship. In whatever form asset specificity takes, the characteristics remain the same. Their uses are restricted to a particular transaction with less economic value in the next best uses (see Williamson, 1996; Klein et al., 1978).

The second variable is uncertainty. The concept of uncertainty can be found in strategic and management literature and refers to an information problem (Slater and Spencer, 2000). In TCE literature, the concept of uncertainty refers to ‘unanticipated changes in circumstances surrounding an exchange,’ MacGuinness, 1994; 70) provided a more specific definition of uncertainty as a condition when ‘there are very many known alternatives or there are known to be currently unimaginable possibilities’ (MacGuinness, 1994; P.70). This implies that there are so many known and unknown possibilities that it is difficult to identify which is likely or not to occur in the future. In the context of contract relation, future conditions of price (Pilling et al., 1984), service or product demand (David and Han, 2004), technology and government regulation (Fitzsimmons and Fitzsimmons, 2006) are few examples of non-contractible ones create potential problems for economic actors to provide for in written contract contracts. Even if it is possible to imagine future contingencies it is not possible to quantify their effect on the contract design. An important contribution to economic contract literature regarding uncertainty is one from Knight (1921). He distinguished risk from uncertainty by noting that ‘risk’ refers to choice situations where decision makers are confronted with conditions whose outcome can be known from alternative choices with known probability distributions and their pay offs. In comparison to uncertainty, risk allows for the possibility that economic agents are able to predict the likelihood of an occurrence and pre-emptive action against it.



The distinction between risk and uncertainty is significant to contract management because Williamson does not consider risk as constraints to efficient contract design but considers uncertainty as problematic to complete contracting design. By contrast, under uncertainty, economic agents cannot plan against future events since the future cannot be predicted with absolute certainty. Even where complete information is available, TCE argues that it is hard for parties to communicate their intentions in such a way that an uninformed third party or a court could reasonably enforce them (Williamson; 1975; 1983). Williamson agreed with Hart (1988) that all long term contracts are necessarily incomplete and has since become the anchor of Williamson's analysis between complete contracting and one incomplete with transaction cost in possibility of future post-contractual negotiations. The uncertainty concept has been extended to cover behaviour of economic agents deemed unpredictable in the sense that individuals may be tempted to play outside rules of engagement or being opportunistic (Williamson, 1985; 1979). The concept of uncertainty and the link to opportunism is important as we examine the contractual problems in PPP and the need for ex-post protection.

Frequency: The last variable of a transaction in TCE model is frequency. In the TCE literature, frequency is understood to mean how often a transaction will have to be carried out between a buyer and a supplier (see Williamson 1979; 1985:60-61). Williamson noted that the frequency with which a transaction occurs matters and argues that where a particular transaction occurs infrequently, (for example maintenance of plants and machinery that takes place once a year) managers will find it cost effective to organise that transaction from outside the firm. This is because the costs incurred to establish a specialist unit that works only once a year cannot be justified in terms of the investments made to keep it operational. In contrast, a manager may find it worthwhile to organise internally a core transaction that occurs frequently and save set-up costs and that of concluding separate contracts for the time the service is required.

Of all the three transaction characteristics, Williamson placed asset specificity at the heart of its analysis which he described as the 'big locomotive to which TCE owes much of its predictive content' in vertical integration. In relation to the behavioural assumptions, TCE hold the view that asset specificity exposes the firm to opportunism where uncertainty is high hence integration is adopted to avoid post-contractual opportunism (Williamson, 1979). This has been subject to many empirical studies and scholarly debate.

One part of research has studied how asset specificity and uncertainty and opportunism affect buyer-supplier relationships and others analyse the effect of these interacting variable on the contract design and governance. Some studies found that asset specificity (David and Han, 2004), others found uncertainty (Klein, 1978) as critical factor that lead to contractual hold ups problems and opportunism. Other writers (Armour and Teece, 1980) contend that if technological uncertainty is high due to quick obsolesce market transaction is predicted. On the other hand if technological uncertainty is due to the complexity of coordinating a technical a system then greater internalisation is predicted (Armour and Teece, 1980).

Although empirical studies suggest that Williamson's assets specificity and uncertainty and to a lesser degree inefficiency provided the rationale for integration, recent debate between Klein (2000) and Coase, (2001, 2006) on one hand and Casadesus-Masanell, and Spulber (2000) on the other suggest that this part of Williamson proposition is not universally accepted.

In recent times, the account given by Klein, et al., 1978) on the Fisher Body and GM as evidence of integration to avoid opportunistic behaviour has been challenged first by Casadesus-Masanell, and Spulber, (2000) and later by Coase, (2006). The view of Coase, (2006 p.268) following the earlier work by Casadesus-Masanell, and Spulber, (2000) on the Fisher Body-GM case and after further investigation now with more access to more documents asserted that ‘asset specificity leading to opportunist behaviour are wrong.’ He continued: ‘The opportunistic actions that were supposed to have taken by Fisher Body, the locating of the body plants, and the use by Fisher Body of inefficient methods of production, never happened’ (ibid). He argued that Klein et al, 1978, got all wrong and that the decision to merge with Fisher Body was purely for business purposes. However, the issue of vertical integration is not the focus of this thesis. Instead, the focus is on the effect of uncertainty which many writers argue causes hold-ups and lead to costly ex post-bargaining in bilateral contracting. The significance of this is addressed later in the thesis in which its economic implications and TCE’s contractual solution of using extra-safeguards prevent parties against the risk of hold ups would be further discussed.

It is noteworthy to point out that we spent greater part of discussing the major contracting problems in business exchanges under two areas of human failings of being limited in our ability to make rational decisions and the possibility that there are dishonest individuals who will take advantage of a party’s cognitive incompetence to cheat. We also note the characteristics of a transaction in which uncertainty on makes long term contract incomplete and when such a relation is supported by transaction specific assets creates scope for opportunism and possibly market failure. All these factors affect bilateral contracting of PPP. From this stage we will be able to address the specific contractual problems associated with PPP and the appropriate solutions. In the next section, we consider the many ways PPP share

similarities with TCE's bilateral contracting and the implication for PPP efficient contract design in terms of risk sharing.

### **2.3.2 Bilateral Governance**

In this section, we look at bilateral governance as a hybrid form of governance. Bilateral governance was a later addition to the original TCE market and hierarchy dichotomy. Williamson (1975) was criticised for paying little attention to hybrid governance modes by over-emphasising markets and hierarchies (Macneil, 1978; Granovetter, 1985). Williamson (1975) dismissed 'hybrid' governance 'as middle kind' that are unstable. However, against the backdrop of the explosion of different forms of hybrid governance of relational contracting (McNeil, 1978); networks (Hakansson and Snehota, 1995; Grandori and Soda, 1995); joint ventures (Hennart, 1991), and strategic alliances (Oxley, 1997), Williamson (1985: 1996) operating successfully in different business sectors, finally accepted and gave legitimacy to it as part of his transaction cost minimisation hypothesis. In accepting hybrid as part of his hypothesis Williamson (1985, p. 83) noted:

'Whereas I was earlier on the view that transactions of a middle kind were very difficult to organise and hence were unstable....I am now persuaded that ... they are much common.'

Unfortunately, hybrid governance has not attracted much scholarly attention and empirical studies in the same way as market and hierarchy, and PPP readily comes to mind which little is understood about its dynamics. At this stage, it would be helpful to examine the rationale behind the increasingly emergence of bilateral contracting despite the fact that transactions that are characterised by some form of idiosyncratic investments, uncertainty with risk of opportunism are supposed to be integrated.

### **2.3.3 Emergence of Bilateral Contracting in Business Relationships**

Although TCE provides that transaction characterised by asset specific and uncertainty are better organised under unified governance to avoid post-contractual opportunism, the extant empirical studies show that bilateral governance is increasingly becoming popular in business activities both within and across national borders (Kogut, 1988; Pisano 1990; Pirrong, 1993).

What accounts for the explosion of hybrid form of governance worldwide?

Some writers in contemporary times assert that in fast and turbulent but dynamic market conditions, organisations are able to survive when they establish collaborative relationships (see also Kogut, 1988; Myer, et al., 1993). Other writers, such as Pisano (1990), explored when firms are likely to enter into collaborative relationships sharing information and managing their uncertainty and found that parties are able to operate successfully in partnerships than when operating individually. His studies discovered that bilateral governance is more likely in situations where partners are in joint product or service development, such as R&D, or where inter-related multiple projects are involved. On the other hand, he also found that bilateral governance will emerge less if there are more alternative suppliers. Pirrong, 1993 found that specialised and capital intensive industries such as the aviation industry, telecommunications or ship building fall into this category. Klein's (1978; 1980; 1996) studies in hybrid relationships found similar reasons. He concluded that bilateral contracting is desirable if the product or the input markets are thin, implying that the relative scarcity of suppliers will mean that the buyers will have to enter into a form of partnership to maintain supply security and exploit their economies of scale for their mutual benefit.

A further consideration case for bilateral governance is that backward or forward integration may not be feasible in some situations because of legal prohibitions Williamson (1985) and Klein (1996) contended in some cases industry regulators had declared integration unlawful on suspicion that it is meant to create cartels for the purposes of seeking monopoly rents. Although in recent times a distinction has been made between firms seeking market power and firms seeking to provide contractual safeguards through sharing and complementing each other's work, antitrust laws mean that bilateral contracting is thriving would continue to be adopted (Shelanski and Klein, 1995).

All the above explanations for the existence of bilateral governance are applicable to PPP. In the public sector as already noted in Chapter 1, bilateral contracting PPP arose as a response to the need to transfer risk to the private sector it cannot handle efficiently and also to access private sector technology and innovation it lacked capacity internally to produce. However, the framing of PPP as hybrid governance meant that the risk of market failures resulting from incomplete contracting (uncertainty), lock-in effects (sunk costs, and switching cost) and opportunism equally apply to and that require that ex-post protection. In the next section, we look at the problem of hold-ups from TCE lenses as it affects public sector in their relationship with the private sector.

## **2.4 Bilateral Contracting and Post Contractual Hold-ups**

In this section, we discuss the literature on contract failures arising from hold-ups, argued to be the biggest challenge in business exchanges (Williamson, 1975; Klein, 1978; Monteverde

and Teece, 1982). A hold-up is the condition where a party finds itself in a relationship detrimental to its interest but in the absence of viable alternatives has to accept less than ideal terms from the other party (see Williamson, 1985; Masten and Crocker, 1985; Masten, 1993).

In the TCE literature, the common causes of hold-ups are occasioned by asymmetrical investments in transaction specific assets as evidenced from empirical studies (see Monteverde and Teece, 1982; John and Weitz, 1988), aerospace components (Masten, 1984), natural gas (Masten and Crocker, 1985), and coal (Joskow, 1985, 1987). Studies in this area also suggest that hold-ups occur when a significant shift in future events affecting the contract relation (i.e. market conditions; technological changes; government legislation) pushes the contract out of the self-enforcement range and the parties need to renegotiate the original terms (see Klein et al., 1978). A classic example of a hold-up is the Fisher Body-General Motors case. The contract between the two parties over delivery of chassis was signed and when demand rose and GM needed to renegotiate the price and volume, Fisher Body refused to locate its production facilities and after costly renegotiations General Motors purchased Fisher Body in 1926. Both TCE theories and PRT have used this narrative to support their theories on the importance of asset specificity residual rights and hold-ups in many textbooks (see Milgrom and Roberts, 1992; Besanko et al., 1996). This version of the explanation for the integration earlier been noted, however, has been challenged contending that the merger has more to do with synchronising their operations than to overcome the opportunistic behaviour of Fisher Body (see Casadesus-Masanell and Spulber, 2000; Coase, 2000, 2006).

In PPP, the problem of hold-ups brings into focus the exit constraints of switching costs. Switching cost refers to cost of writing off previous investments made and cost of developing

a new supplier in the market. Switching costs may go beyond writing off previous specific assets. Cost such as searching for a new supplier, delays in project completion, service interruptions and loss of reputation and payment of compensation are some of the obvious cost associated with switching from one supplier to another (see Heide and Weiss 1995; Blankerburg et al., 1999). A further consideration is also given to loss of future revenues a period between termination and the time that the new supplier becomes operational. Essentially, switching cost could be prohibitively high in PPP. For example, in the NIRS2 project in the UK, the estimated switching costs were £44 million (Lonsdale, 2005a). This leads us to consider what another cause of a hold-up termed ‘fundamental transformation’ arising from long term relationship in business exchanges.

Williamson also draws attention to a phenomenon of ‘fundamental transformation.’ The term refers to the situation whereby suppliers will go through competition bidders but in the next contract renewal the buyer may no longer be interested in changing partners by using the market as a result of dedicated assets deployed since the last contract award. Williamson (1976) used this term to describe the Oakland California cable TV (CATV) franchise. He found out that the franchisee considered it costly to write off the dedicated investments and use the market again to select a partner there was prepared to accept terms that were no near the original one. However, the ‘small number relation’ is not restricted to the franchise industry but in other sectors where dedicated assets to support a relation is required. In the IT sector, for example, Lacity et al, (1996) examined broadly long term contracting effect on IT contracting. These writers concluded that this high asset write off prevented the IT buyers from re-entering the market during contract renewals. Another perspective than can be taken is that some suppliers may encourage IT buyers to invest in their systems and effectively cut off other competitors and lock them into their systems. Theoretically, either the buyer or



supplier could engage in hold-up behaviour and opportunism. Although opportunism may be present in buyer supplier exchange, it could be a real risk if the transaction involves asset specificity. This is because it allows the vulnerable party to be exploited.

In PPP contracts, the public sector is vulnerable hold-ups in similar way since most of the relationships are characterised by medium to high asset specificity (Lonsdale, 2005a). One of the problems facing the public sector is uncertainty and is the major cause of hold-ups in PPP. Empirical results in UK public sector shows that uncertainty relating to incomplete specification of all future contingencies end up with high transaction costs and poor value for money. For example, the Benefits Agency (UK Treasury Task Force, 1999), Channel Rail link (Glaister, 1999) and Libra project are but a few of the many other high PFI projects (see; NAO, 1999; Treasury Task Force, 1999; Gaffney and Pollock et al., 2001; Lonsdale, 2005b; Sadka, 2006).

From the above cases, one can argue that many of the hold-ups the public sector faces are attributed to uncertainty with economic consequences of high transaction cost and poor value for money. This is particularly so, at least, from TCE perspective, an opportunistic private supplier may take advantage of a hold-up to appropriate economic rent from the relationship. This does not suggest that all suppliers are potentially opportunistic and nor does it also suggest that no supplier will be opportunistic. Perhaps, more often the risk posed by hold-ups can result in vulnerable actors to seek partners who are not opportunistic. However, this is proven difficult in practice because of behavioural uncertainty on the part of economic agents of detecting potential opportunistic suppliers.

Despite the central problem of hold-ups and the risk that opportunistic suppliers exploit to appropriate quasi-rent many writers challenge the view that hold-ups are orchestrated by suppliers or that it result in economic rent appropriations (Klein, 1996; Coase, 2006). As already noted Klein does not share Williamson's assertion that economic partners engage in strategic behaviour to engineer hold-ups for rent appropriation. Klein, 1996) shown that the hold-up that occurred in the GM-Fisher contract was a result of uncertainty when the original contract shifted from self-enforcing range to conditions not covered in the original contract. He further distinguished between a normal hold-up situation where a partner issues of threats of exit and the one which it is used a party to negotiate favourable terms against the ideal position of the other part. While supporting arguments that hold-ups occur in business exchanges and can also affect firms' performance, Coase, (1991; 2006) demonstrate that the presence of hold-ups in a relation does not indicate economic exploitation in the A.O. Smith contract with GM (Coase, 1991, p, 71-72). Demsetz, 1982; Hubbard, 2001 also show that hold-ups may be subtle and difficult to detect.

Given the problem of identifying a potential opportunistic suppliers and the effect of opportunism on optimal outcomes, buyers are advised to assume the worst and design an efficient contract to protect themselves from possible post-contractual opportunism (Williamson, 1975; 1983). This takes us to consider TCE guidelines on the use of credible contract enforcement mechanisms by buyers can craft into their contract design to protect themselves against uncertainty and post-contractual opportunism. Before we examine Williamson's (1983) credible commitment model and its substantive application in transactions supported by dedicated assets, we discuss briefly private mechanisms considered as alternative to explicit contracts and the role of repeated interactions in changing uncertainty into calculated risk between short term opportunistic acts and towards long term

to contractual mutual benefits and which is relevant in our study.. In the next section we look at these approaches.

#### **2.4.1 Approaches to Contract Disputes Resolution**

Contracts are normally supported by contract law and that means contractual disputes can be subjected to court arbitration and litigation. While this can be useful using third parties to settle commercial disputes, a growing criticism from writers suggests that it could be counterproductive in relationships such as PPP where continuity is deemed important (Williamson, 2000; 2003; Mahoney, 1991). Writers such as Klien (1978), Telser (1981) and Mahoney (1991) have argued against the use of the courts as it is found to increase transaction costs through delays and high legal fees. Moreover, many writers (e.g. Tesker, 1981; Mahoney, 1991) have argued that if the courts fail to enforce the terms literally, then this may paradoxically create more scope for hold-ups and this in turn would mean that parties may be cautious in what they write in their contract.

The obvious difficulties of using the courts to settle contractual disputes allows parties to seek protection using reputations and repeated transactions (Williamson, 1979; Mahoney 1991). However, as has been found in practice, there are some problems with the reliance on the goodwill of partners to remain committed to non-enforceable contractual promises. In the case of reputation effects, it is believed it can act as an effective check on opportunistic behaviour as past performance is a key criterion for future business. Studies have shown that mere reputational effects are insufficient to enforce contract performance (see Williamson, 1979; Gallick, 1984; Coase 2006, p). For example, Gallick (1984) study of the fishing

industry in the USA showed that when fishing technology changed and short-term gains become attractive, the processing company reneged on exclusive dealings. The argument is made that, reputation was no longer an effective enforcement mechanism.

Closely related to agents' reputational capitals is the use of contingent renewal as a tool to enforce good behaviour (performance) of economic agents in return for future business (Telser, 1981). As Gintis (2005) found out, in contingent renewal markets the principal has power over agents because they can impose cost on agents by terminating their services that persistently fall below expectation. The strong point for this approach is that suppliers are compelled by risk of loss of future earnings to behave responsibly. However, the limitation in the use of power of contingent liability hinges on the fact that alternative sources for the supply for those particular goods or services might be in short supply. In such circumstances, Gintis (2005) noted the supplier may exercise counter-threats on the buyer by withholding its valuable services or products (see also Telser, 1981). Moreover, the strength of this approach also hinges on whether the supplier can easily develop alternative markets.

Another informal approach often mentioned in the literature is repeated game. Similar to contingent liability, parties are disposed to collaboration for mutually satisfying outcomes and may be willing to share private information for their common good and survival. However, as has been pointed out, prisoner's dilemma phenomena tend to frustrate the use of this model. A prisoner's dilemma exists when individual incentives will lead them to the worst outcomes possible for themselves (see Gintis, 2005). However, uncertainty on what action other party may take may incline them to act opportunistically on the logic that if he does not cheat, the other party may do so, leaving him worse off. Moreover, repeated game

theories can be economically wasteful, because parties will incur more transaction costs to out-guess each other (Gintis, 2005).

In the case of formal written long-term contracts, some writers (e.g. Klein et al., 1978; Joskow, 1990; Lusch and Brown, 1996) provide justification why this strategy might be useful in providing partners with stability or safety nets against post-contractual opportunism. While it is found that exclusivity time given to investors allows for sufficient time to recoup investments, studies show risk of hold-up makes this approach unsuitable in many transactions characterised by uncertainty. Some market conditions, such as price, demand and technological changes are difficult to predict over the contract planning period but could cause tensions in the relationship should they occur. Moreover, tight contract terms may create opportunities for parties to engage in a hold-up by insisting on the literal interpretation of the contract when unforeseen contingencies arise. This is what actually happened in the GM-Fisher contract when the conditions went out of the self-enforceable range as a result of events not foreseen and provided in the contract (see Klien et al., 1978).

The above approaches and their weaknesses have implication for public sector managers. The reason is that adopting reputations and repeated transactions are private agreements and may be convenient and cheap but it leaves the fate of the relationship to chance since these mechanisms are unenforceable. Even if the courts can enforce contractual performances, the public sector might not be keen to adopt litigation since delay and cost will affect disruptions to essential services being provided by the government. On the other hand, using non-legal enforceable arrangements to support relationship alignment will not be a problem if opportunism is not present. However where opportunism exist the use of non-enforceable

informal agreements may be counter-productive. This is because suppliers may be tempted to act dishonestly if gains from short term opportunism are higher than long term contractual compliance. Williamson (1991, p.273) stressed this point strongly when he commented that: 'When the lawful gains to be had by insistence upon literal enforcement exceed discounted value of continuing the exchange relationship, defection from the spirit can be anticipated.' As a result, the solution to this conundrum for the public sector is on the reliance of Williamson's prescription to craft appropriate credible commitments as extra-safeguards to protect themselves against this problem of uncertainty. In the next section we examine the assurance given by Williamson that the public sector managers apply credible commitments to share risk efficiently to minimise transaction costs.

#### **2.4.2 The Expectation of Balance: Bilateral Governance Shared Investments or use of Financial Hostages**

The similarities between PPP and bilateral governance of TCE mean that the relationship between the public sector and the private sector also involves asset specificity and uncertainty and risk of hold-up. TCE examines the problem of asymmetrical asset specificity and noted that contractual problems might exist when economic generating assets are not jointly owned or risk shared. Consistent with Grossman and Hart, 1986 and Hart and Moore (1990) PRT model, TCE recognises the risk of post-contractual opportunism if transaction assets are not shared equitably. The concern from both traditions join in their beliefs that if the economic generating assets are owned by an individual say the buyer, the supplier will not necessarily take the assets' long run value into consideration and may appropriate the stream of rents especially when there is information or measurement problem Kim and Mahoney (2005). A

fear that an opportunistic agent will dishonestly appropriate all gains from relation may impact negatively on the economic activities. One of the drawbacks to economic activities is that parties may be unwilling to invest in transaction specific assets to support a relation unless they receive credible commitment that the other party will not behave opportunistically (Grossman and Hart, 1988; Grossman and Moore, 1990. However, if the contracts are complete from agency perspective then it is possible for owners of the assets to anticipate the other party's opportunistic acts and craft every contingency into the contract in such a manner that the initial contract balance will remained unchanged even during post-contractual negotiations over the life of the contract. As pointed out by Kim and Mahoney, (2005) based on its assumptions the separation of ownership from control of economic assets does not matter in agency framework.

A widely recognition that managers are bounded rationally and uncertainty makes contract incomplete means that all future contingencies cannot be specified in contract. The renegotiations over the non-contractible elements have been shown to cause efficiencies problems in sharing gains from the output. As a solution to this problem, Williamson (1983) provides two strategies to craft extra safeguards to balance the risk and uncertainty in the relation. In the first option, where the public sector has made more investment in transaction specific than the private sector, which often the case, according to TCE, the investments should be shared with the private sector. In a situation where it is not practicable to contribute equally to dedicated assets, the buyer is advised by TCE to demand financial hostages equal to the risk not covered in the relationship. It is typically argued that if risk in dedicated assets is shared equitably both parties will have incentives to respond to emerging events and manage their uncertainty in mutual satisfying way. On the other hand, if one of the parties, and if it is the buyer, who has invested more in the relation, will bear more of the risk than the

supplier. The problem for the buyer is that he gets locked into the relation with the effect of getting exploited by the supplier.

Clearly, TCE prescription appears to be more appealing and suitable to the public sector as well as private businesses. However, the task of selecting the appropriate credible contract enforcing measures to optimal contract design appears to be difficult, given that decision-makers are assumed to be rationally bounded (Simon, 1957). Williamson responded by introducing the concept of farsighted contracting that makes buying managers having the ability of exercising foresight to select broad contractual safeguards to develop and sustain post-contractual balance. Williamson stressed the point that although buying managers might be rationally bounded they are not necessarily myopic and argued that the economic agents have the capacities 'to learn and to look ahead, perceive hazards, and factor these back into the contractual relation, thereafter to devise responsive institutions' (Williamson, 1996, p. 9). What Williamson is arguing is that buying managers have the unlimited contractual foresight to recognise specific risk arising in a relation have the ability to provide contractual protection against it (Williamson, 1983, 1985). From TCE reasoning post-contractual lock in could be avoided and most importantly, result in interdependence or contractual balance. Table 2.2 shows the three generic governance choices for transactions characterised with little or no asset specificity to high significant levels of asset specificity and their economising behaviours are summarised in which farsighted contracting is emphasised under bilateral governance. It is to be observed that the introduction of feasible foresight appears to address the bounded rational contradictions to provide strong arguments for the prescription of credible commitments.



**Table 2.2 Summary of Organisation Choices and Balance**

	Transaction Characteristic	Economising Behaviour
Market Governance	Spot buying –	Market Forces market sets the equilibrium prices and functionality (high powered incentives)
Hierarchy	High levels of asset specificity and uncertainty	Bureaucratic control and ownership (Fiat and forbearance law)
Bilateral Governance	Medium to high asset specificity and uncertainty	Farsighted contracting : Use of hostages or shared investments use of farsighted contracting )

Adapted from Mechanism of Governance (Williamson O. E., 1996).

The significance of this is that while this allows for the development of a theory that bridges the conceptual gap between incomplete contracting and complete and deterministic contract design, less is known about how this can be operationalised by public sector buyers. We examine the empirical evidence of how successfully this has contributed to the development of balance in bilateral contracting

### **2.4.3 Evidence Provided by TCE for Bilateral Balance**

Several studies have investigated whether credible enforcement arrangements have resulted in contract design. Early empirical support came from the franchising industry. An important study conducted by Hadfield (1990) on the role of credible commitments found that the exchange of hostages sustained a balance relationship between franchisees and the franchisor (see also Klien and Leffler, 1981; Kaufman and Lafontaine, 1994; Minkler and Park, 1994; Zupan, 1989; Brickley, 1999). Other studies in the marketing channel found evidence that

sales agencies successfully used offsetting investments in other specific areas of the relation to reduce their dependence on the powerful manufacturers to some extent in the automobile industry (see Heide and John, 1988; Oxley, 1997; Allen and Philips, 2003).

In the case of PPP, public managers in UK are encouraged to follow TCE guidelines to craft extra-safeguards such as the use of financial hostages to manage their risk but these results in mixed results. While some studies found evidence of symmetry between the public sector entity and the private partners (Bigelow, 2001; Nickerson and Silverman, 2003), other studies (e.g., Pollock et al., 2001, Parker and Parker and Hartley 2003) reported that the public sector was in asymmetric relationships and suffered from poor supplier performance. In a recent study, Lonsdale showed that the IT contract between Siemens Business Services (SBS) and National Savings and Investments (NSI) was balanced post-contractually as a result of exchanging financial hostages while on the Libra project; the Benefits Agency and NIRS2 contracts among other PPP projects the public sector failed to create balance with the private sector entities with the added problem of high transaction costs (Pollock et al., 2001; Spackman, 2002; Sheil, 2002; NAO 2003c; Lonsdale, 2005a. Thus it appears from the above empirical cases show that there are many things about PPP largely uncovered by research.

## **2.5 Concluding Comments**

This chapter has reviewed the analytical role of the TCE framework in explaining how a contract can be managed to achieve optimal contract design. Williamson identified bounded rationality, opportunism, asset specificity and uncertainty as the main source of market

failures and transaction cost (Williamson, 1996). The insight from TCE theory is that economic actors are rationally bounded to design complete contracts and this becomes more complicated if the relation is supported by transaction specific assets in the presence of opportunistic suppliers. This has profound implication for managers in the public sector using PPP route for public provision. However, Williamson provides contractual solution through his credible commitments.

A study of UK policy guidelines regarding public-private business arrangements shows that much of the public managers' expectation to use farsighted contracting to design credible commitments into their relation to achieve a balance grows out of the TCE's expectation of bilateral balanced assumptions (OGC, 2002; PAC 2003a). While the efficacy of credible commitments model cannot be denied, there is also cause for concern given the mixed results from empirical studies. The concern is that there might be some unexplained factors accounting for asset specificity responsible for the observed asymmetrical relationship in PPP but largely remains unknown. Moreover, the TCE framework somehow has not completely explained the continued public sector asymmetrical relationship with the private sector and most research work turn to the obvious explanation using the old worn cliché of asset specificity to account for the asymmetrical relationship in PPP and has paid little attention to the possibility that hold-up can occur when no dedicated assets are involved in the transaction. Little is not known yet about this and there appears to be a gap in TCE framework and analysis. This lack of complete explanation from TCE provides us with the impetus to investigate the issue of balance in PPP by using the power theories. This in turn, might help us find the explanation for the difficulties faced by public sector managers in their efforts to apply TCE prescription to balance their relationship with the private sector. In the next

chapter we examine this weakness in detail and use the insight to design our research theoretical model for our study.

## **CHAPTER 3**

### **POWER AND CONTRACTUAL BALANCE**

#### **3.1 Introduction**

In this thesis so far, we have established the prevalence of PPP, noted its drivers, and made the link between PPP and TCE, especially balanced bilateral contracting. We also looked at the some of the literature that has explained the balanced bilateral contracting theory and found it to be supported in various cases. In this chapter, we look at the various criticisms of TCE. We examine first general criticisms of TCE in section 3.1, followed by specific criticisms of TCE's approaches to bilateral governance. Section 3.2 discusses power and Section 3.3 discusses Resources and Capabilities in negotiations. This leads the author to argue that the ability to develop balanced bilateral governance can be hampered by two factors: pre-contractual power resource, asymmetry in resources and capabilities in negotiations. Finally, it introduces the conceptual framework emerging from the research and provides supporting evidence from the study.

##### **3.1.1 General Criticisms of TCE**

Whilst TCE has clearly provided great insights into business-to-business relationships over the past 30 years, it has also been subject to criticisms and extensions over a wide range of issues, many of them about its behavioural assumptions, and, more generally, about transaction cost analysis. The initial criticisms of TCE's behavioural assumptions were

particularly severe. Early critics described the notion of opportunism as ‘controversial’ (Granovetter, 1985; Donaldson, 1990; Ghosal and Moran, 1996a; Conner and Prahalad, 1996) and bounded rationality as ‘inconsistent’ (Hodgson, 1991; Bröder, 2000). Others have also criticised the TCE model as ‘unhealthy’ (Hirsch et al., 1990), and an ‘ethereal hand for organisation researchers’ (Donaldson, 1990). Probably, the severest criticism came from Ghosal and Moran (1996a; 1996b) who described the TCE model as ‘bad for practice’ and without “realism and balance.’ Ghosal and Moran’s argument was that TCE theory had ignored the distinction between markets and firms in terms of their internal logics, and therefore failed to appreciate ‘that managing an organisation based on the logic of markets prevents the development of organisational advantage’ (1996, p.58).

Further criticism from the trust based schools in relation to opportunism assumption. According to the trust-based school of thought mutual ex-ante fear of rent seeking behaviour and opportunism has led to reluctance of parties to invest in specialised assets. It is typically argued that positive human traits such as trust could be cultivated to support business relationships could better be managed successfully even at higher levels of asset specificity (Grandori, 1995; Noteboom, 2002).

All the above critique directed at TCE framework are but few of the many in the literature but, at least, demonstrate clearly some of the weaknesses in its assumptions. However, what is most important to this thesis is a specific question that has engaged the attention of both practitioners and policy makers in the public sector. This is whether the bilateral contracting mechanism can be balanced by the public sector as easily as is suggested in the TCE.

### **3.1.2 Incentive Theories and Procurement Functions**

In Chapter 2, we noted that PPP is characterised by incomplete contracting and therefore subject to hazards of hold-ups and supplier opportunism. We also noted TCE's contractual solution of shared investment in dedicated assets or the party at risk demanding financial hostages from the other party. In UK, government officials have followed TCE's prescription to manage its partnership with the private sector. For example, UK, the National Audit Office (NAO, 2005b, p235) report on London Underground made some recommendations to policy makers that; 'success (in PPP) requires a genuine alignment between contracting parties to ensure that the partnership is more than just a statement of intent' Similar recommendation came from the UK Public Accounts Committee (PAC) and HM Treasury that 'PPP needs to be approached in the spirit of partnerships, where both sides are open, share information fully and work together to solve problems' (Public Accounts Committee, 2003a p.3 quoted in Lonsdale 2005a).

This optimism has also found its way into policy documents of the World Bank and other international developing agencies like the (World Bank, 2004b; OECD 2008). As we noted in Chapter Two, empirical evidence does not conclusively support the assumptions that PPP could easily be balanced. The mixed results however, suggests that TCE logic is limited in its ability to explain the contradictory results and throws open the question about the soundness of the underlying assumptions on credible commitment model. In view of this we re-examine assumption underlying the credible commitment and the confidence it reposed in buying managers to achieve a balance in the design of the contract. We start by taking a critical look at the incentive theories in economics on efficient contract design in specific context of PPP.

The TCE theory has similarities with agency theories PRT perspectives (Williamson, 1975) in many aspects in the context of how economic agents can support their business relationships with efficient contract design in the form of protection against risk of hold-ups and post-contractual opportunism. Whilst, agency theory prescribes for risk-incentive approach against uncertainty arising from information asymmetry, both PRT and TCE recognises the problem of property rights and prescribes for efficient contractual solution to protect parties against the problem of uncertainty and hold ups (Williamson, 1979,1983; Grossman and Hart, (1986) and Hart and Moore (1990).

However, the optimal contract mechanism of incentive theories can be interpreted as ignoring the distribution of resources endowment of the parties. In other words, TCE, PRT and agency theories paid little attention to the issue of power in business exchanges. This omission in procurement context means that the incentive theories are limited in their ability to explain the differential power that naturally arises when parties with different needs but are in possession of critical scarce resources decided to engage each other in an exchange relationship i.e. procurement environment. Although PRT recognised the importance of scarce resources and the ownership right to earn income, it failed to consider that supply and demand constraints may create an advantage for one party to have power over the other party. In the case of agency theory, it pays little attention to property rights system in which agency problems occur, thus the effect of competing over scarce resources was ignored in their analysis. Briefly, it can be argued that incentive theories provide us with only partial understanding of contractual problems and solutions in buyer-supplier exchange relationship.

Having said that what is conspicuously missing from the three models and in Williamson's TCE model in particular, is power. Williamson made some assumptions when proposing his



credible commitment model which are relevant in the studies of PPPs. They are discussed in the next section.

### **3.1.3 TCE Assumptions on Credible Commitments**

Williamson made a number of assumptions including a world in which buyers and suppliers have equal capabilities and resource endowments and these are evenly distributed between economic actors and business to business relationships. Although Williamson (1995) accepts that the concept of power is important in politics, and to some extent in intermediate markets, he does not think that power is relevant to the distribution of risk and value in an exchange relationship. His thinking is grounded in the mainstream economist's view of the market as a perfect mechanism where efficiency of exchange is assumed to be achieved through the coordination of the independent actions of multiple actors in the market. In this world of TCE, economic actors have the ability of economising on bounded rationality and opportunism.

As a result, TCE theorists have argued from several fronts contending that business-to-business relationships have efficient internal self-regulatory coordination systems to create equilibrium. Even if market inefficiencies such as power and opportunism exist it is assumed that could be competed away by many participants in the market. Consequently, Williamson, 1995, p.23) dismissed power that: 'Power has little to contribute to the study of contract and organisation in circumstances where the parties to an exchange can and do contract in a relatively farsighted way.' This demonstrably sums up how TCE researchers have come to downplay the role of power relations in buyer and supplier relation. From this perspective, it can be argued that the feasible contractual solutions to contractual problem are partial

because they do not take into account set of constraints in buyer and supplier exchange relationship. The problem with these set assumptions is that Williamson takes the private sector's attitude towards risks as neutral. Based on this narrow view, Williamson did not consider the possibility that a supplier may have the ability refuse to c-operate with the buyer to craft credible commitments into the contract designed aimed at reducing its scope to maximise profits. The above critique is one of many we shall be exploring as we develop our argument in the subsequent sections.

### **3.2 TCE and Power**

Writers of the power relations school have challenged Williamson's views on power in business-to-business exchanges and argued that business exchanges are often characterised by the power relations (see Heide and John, 1988; Cox et al., 2000). Some writers found power as significant influence in supply chain management, health and construction sectors (see Cox et al., 2001; Lonsdale, and Watson, 2004). As these and many other growing empirical studies show that power is relevant issue, some researcher turned their attention to power and dependency theories.

Based on above, this thesis proceed from the premises that if Williamson's assumptions on power are relaxed would lead us to consider transaction costs in an imperfect market which can equally constrain efficient contract design. In a recent study Hingley (2005, p.552) paid attention to power and found power imbalance in UK fresh food supply industry and contended that 'the concept of power is rarely discussed in supply chains except to deny its importance' and recommended that power relation variables should be considered in buyer-supplier analysis A study into the problems facing PPP pointed out that public sector

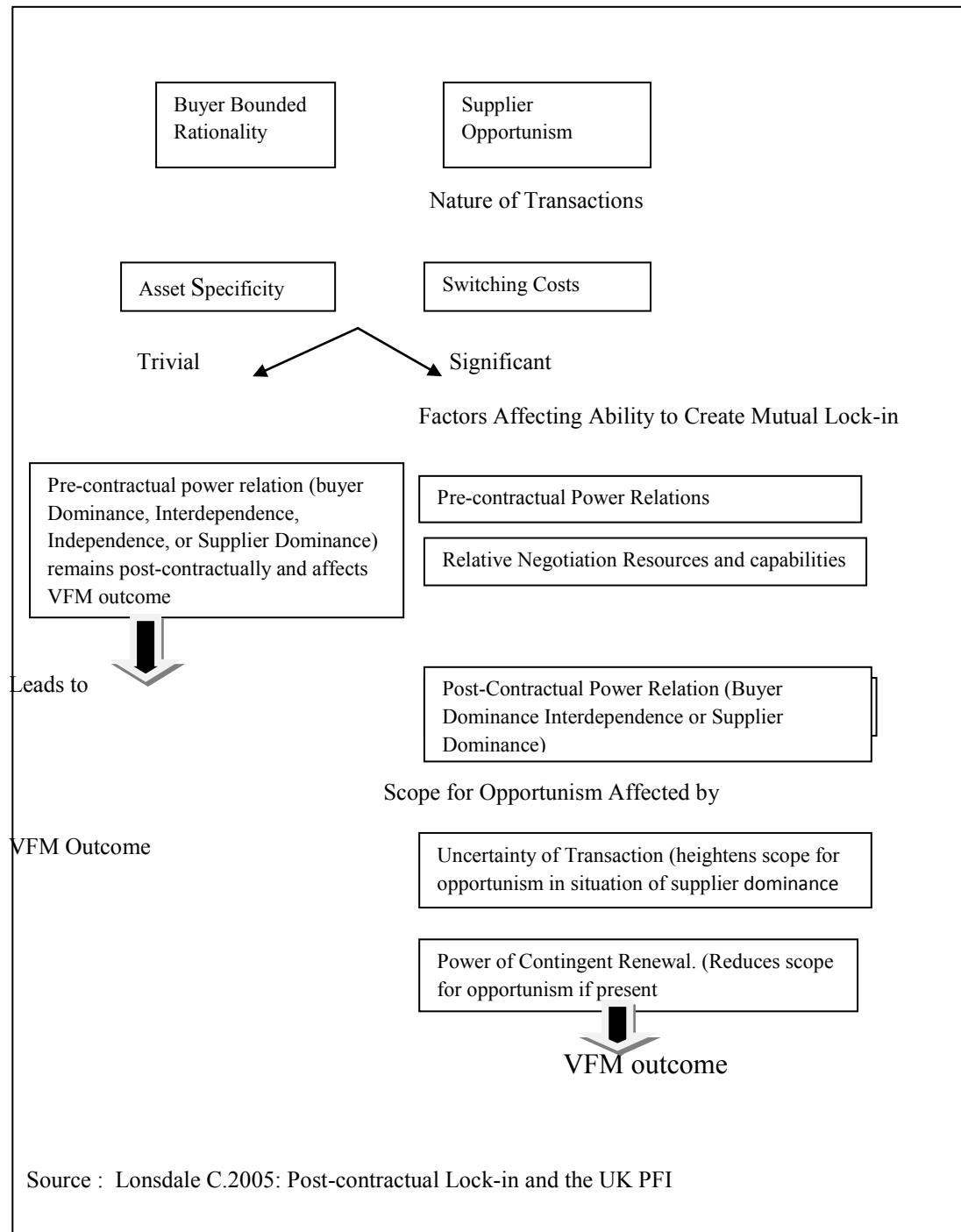
contracting the private sector for strategic services put private service providers in a power advantage to leverage for good deals at their expense (Lonsdale, 2005b).

Perhaps the two UK PPP contracts of National Savings and Investments (NSI) and Lord Chancellors Department (LCD) studies by Lonsdale, 2005a), is the most outstanding example of providing different circumstances a public sector entity succeeded in crafting credible commitments into the contract design and the other entity being hampered by adverse pre-contractual power relations to craft credible commitments into the contract design.

In the case of NSI and Siemens Business Systems (SBS) on one hand and LCD and ICL on the other, Lonsdale demonstrate that while the NSI, a public sector body, was able to successfully develop and sustain a balanced post-contractual relationship with its supplier, the other public sector entity, LCD, found itself in an adversarial relationship and, as a consequence, failed to achieve a balance.

Lonsdale, (2005a) also found that the relative asymmetry in the resources and negotiation capabilities with the private sector allowed the private sector to outwit the public sector in the negotiations. His third factor is internal politics in procurement decision-making. He argued that procurement managers in public face are constrained by the preference of managers higher up the hierarchy ladder who may use their power position to override sound procurement decisions leading to poor contractual choices-a problem highlighted in the organisation literature (Pfeffer. 1978). Based on his findings Lonsdale (2005a) consequently proposed a model to study PPP performance in creating the right conditions for successful risk transfer to occur (see Figure 3.1). He observed that given the nature of essential nature of

**Figure 3.1 Framework for Assessing the Scope for Risk Transfer**



projects that come under PPP the public sector face tremendous obstacles to develop post-contractual balance with private sector suppliers and that in turn affects its ability to get good value for money.

In reviewing his arguments in the NSI/ SBS and LCD/ICL cases, it became obvious that the adverse pre-contractual power relationships and asymmetry in resources and capabilities of negotiation were found to have significantly impact on the efficient contract design. Regarding internal politics in procurement decision-making it is not clear how that led or facilitated scope for lock-in in either of the two cases of SBS and LCD contracts and other ones he investigated. In drawing his conclusion and in an attempt to link internal politics to post-contractual balance Lonsdale, (2005b, p.242) noted that: 'Such contracts are far from ideal in terms of contract management as they are inevitably vague-given the level of uncertainty characterising such long term contractual periods- geared towards an expectation of renegotiations.' It does appear that the writer is substituting uncertainty in decision-making for internal politics in decision-making. Although it could be argued that personal preferences of people in authority may get in the way of efficient utilisation of scarce resources and thus may be relevant in understanding the political implications of stakeholders in the implementation of PPP policy it does not address the specific problem of balance in a relationship. In this instance, although Lonsdale attempted to explain contractual hold-ups or its absence by looking at internal politics he failed convincingly to link it to the problem of contractual imbalance or hold-up. In addition, introduction of internal politics in this study may throw the purpose of this study out of course into political economy literature which is outside the scope of this thesis. Moreover, when contract decisions are taken by the political authority or outside the procurement department, the act of crafting efficient extra-safeguards into the contract relation is the responsibility of the public procurement department or the negotiation team which this thesis is investigating its impact on the contract design. Also, review of the PPP policy choice is vested in the power of seat of government in Ghana and not within individual public sector entities as is the case in developed countries. For the above reasons, this study is focusing on investigating the two independent variables

of adverse pre-contractual power relation and asymmetry in resources and negotiation capabilities. Our next task is to review the literature with the aim of first, to establish whether Lonsdale proposition is grounded in literature and, second, to find out if it has any research value in order to carry out empirical research in a different country ie in Ghana. The next section reviews the literature on power focusing on the variant power-dependency theory and relations.

### **3.2.1 Pre-Contractual Power and Contractual Balances- Lonsdale Factor**

The notion that the concept of power is an inextricable factor in business exchanges has long been advocated in the social science literature (Emerson, 1962; Dahl 1957). In network exchange theory, power in social exchange denotes inequality in society. According to the early power literature, wealth arose not primarily from money but from exchange value or power of exchange. Marx (1848), an early proponent of power, argued that power enabled entrepreneurs to control the factors of production and exploit labour, leaving them to live like wage slaves.

In contemporary times, the discourse on power has expanded into social exchange theory.

In social exchange theory, it is assumed that some actors control more highly valued resources than others and the differences in the nature of resources among people leads to exchange and interdependence. One of the most prominent contributions to the analysis of social power was Emerson (1962, 1964). In the early development of the power-dependence

theories, he postulated that inequality in resources can lead to power and inequality with the weaker party in subjugation and the powerful in domination (see also Blau (1664, 1986).

Emerson, (1962, p, 32) in his classical power dependency model stated the dependence of A on B, in turn is a direct function of the motivation investment of B in goals mediated by A and a negative function of the availability of those goals to B outside the A-B relation. Emerson shows that in an exchange relation between two actors, A and B, the power of an actor increases as its value offering to the other party increases and decreases proportional to the degree of availability of the other party to seek alternative sources. Thus the resource value and resource availability determine the level of dependence in A-B relation. The more dependent B is upon A, the more power A has over B (Emerson, 1962; Pfeffer and Salancik, 1978; Cox et al, 2000).

Essentially, what this means is that if A depends on B more for valuable resources than B on A then B has power over A. Some scholars have subsequently developed the power dependency theory by introducing variations to define power relations in buyer-supplier business exchanges (see Pfeffer and Salancik, 1978, Krajić, 1983; Cox, Sanderson, Watson, 2000). The common thread running through their models and empirical studies is that power in exchange is derived from the relative dependency of exchange partners on one another for the resources of value they desire. For example, Buchanan (1992) conceptualise power dependence as different in value that buyer-supplier attaches to the relationship.

In other words, the fundamental assumptions of all the developed models seem to emphasise the occurrence of power structure in buyer-supplier and those characterised by asymmetrical

inter-dependences. The asymmetrical inter-dependences may be dysfunctional because the dominant partner may attempt to exploit the dependent party (Emerson, 1962). In that sense one can argue that parties bargaining power may be derived from critical resource endowments that a party holds.

Following these early developments on resource and dependency, some researchers (Cox et al., 2000) developed model to study power in buyer-supplier relations. The model is similar to Emerson model in that the model employs comparable endowment resources of utility and scarcity dimensions to derive power structure predictions. Utility refers to the importance of the resource to the other party's operations. The more a party values a particular resource, the more he becomes dependent on the party who is in possession of it. Scarcity, on the other hand, refers to the level of difficulty in gaining access to alternative sources of the valued resources outside of the relationship. Others looked at imperfect substitution as critical asset at price (Martimort and Stole, 1999). A third element, information, is then added by some members of the power relation school. According to Cox et al (2000), control or access to right information is considered as a power resource it comes to contract negotiations. MacDonald, (1999) noted that access to information enjoys pricing independence. Thus we can identify the three elements of utility, scarcity, and information represent the sources and structure of power in business exchanges (Cox et al., 2000). The model developed by Cox et al, (2000) is shown in Figure 3.2. An alternative scenario in the matrix is that the two parties can be independent of each other. Finally, they can become inter-dependent, potentially sharing gains and losses in an agreed, mutually- beneficial manner and finally one of the parties can become the dominant.



**Figure 3.2 The Four States of Pre-contractual Power Relation**

Relative utility and scarcity of buyers' resources to the supplier	A Buyer Dominance (no scope for co-op gains)	B Buyer-supplier Interdependence
	C Buyer-supplier Independence	D Buyer Dependence (no scope for o-op gains)

Relative utility and scarcity of suppliers' resources to the buyers

Source: Cox et al 2000

From the above power construct it is possible to draw three central assumptions.

- (1) Economic actors engage in an exchange to obtain resource of value hence mutual dependence develops.
- 2) Exchange partners behaviour is motivated by the desire to increase gain and to avoid loss
- (3) actors engage in business exchanges obey demand and supply characteristics.

These core assumptions allow various predictions to be made about the behaviour of actors engaged in exchange and the effects of different factors on the outcomes of exchange (see also Mohm, 1997; Molm and Cook, 1995; Cox et al., 2000).

### **3.2.2 Impact of Power on Surplus Value**

The relative power of buyers and suppliers are expected to be a key factor in explaining the value capture. Surplus value simply refers to the difference between the supplier's costs and

the value of the product to the buyer (Cox et al., 2000). Although both the public sector and the private sector may have common desire to be in collaboration, the literature suggests that goal conflict exist in terms of maximising their share of the value from the relation.

The writers (Cox et al., 2001) further contribution to value capture in business relationship is a model developed to explain six possible feasible generic relationship styles that are likely to emerge in the distributing of gains from collaboration from power perspective. The six feasible generic styles are depicted in Figure 3.3.

**Figure 3.3 Generic Buyer and Supplier Relationship Types**

Distribution of Surplus value Created from the Relationship	Adversarial Arms-length 1	Adversarial collaborative (Buyer Dominance) 4
	Non-Adversarial Arm's-length 2	Non-Adversarial collaborative (Inter-dependence) 5
	Adversarial Arms-length 3	Adversarial collaborative (Supplier Dominance) 6
	Arm's-length	Collaborative

Source: Robertson Cox Ltd (2001). All rights reserved. Adopted from Cox et al 2002

The relationship matrix suggests that if the buyer is in total dominance then the buyer stands a good chance to maximise its share of the surplus value (top row). On the other hand, if the buyer is in a dependent position vis-a-vis the supplier, then that dependence will act as a

constraint on the ability of the buyer to achieve its benefit target from the relationship (bottom row). The situation is different if both parties are in an inter-dependent or balanced power relationship. In that case, both the buyer and supplier have incentives to share the surplus value in a mutually satisfying formula (middle row). Studies in PPP suggests that most of the contracts signed by public authorities with the private sector are located in boxes 3 and 6 of the matrix in Figure 3.2, indication of adversarial relationships with the private sector, implying that the public sector may found itself in an asymmetrical position and yet remain in the relation

From the above analysis, it is reasonable to assume that power and dependency underpin public sector and private sector business relationship. Like all market exchanges, bargaining process entails the passing of value from one individual to the other in exchange for what the other party's values. However, the relative value a party attaches to a resource differs in a relation in exchange for another. In relation to the public sector, the problem of power structure can be argued that since the public sector has less sufficient resources to meet their need and have to rely on the private sector for valuable services to meet public provision requirements and the private sector depends on the public sector for business and profits thus interdependent relation pertains. However if the public sector depends more on the private sector than the supplier on public sector then the public sector will struggle to develop inter dependent relations. This difficulty has been commented by Lonsdale that: 'it will be extremely difficult to get a supplier in developing contractual safeguards that will create balance in the post-contractual relationship' (Lonsdale, 2005a, p.238). Even though the above power discussions throw more light on the dependency, little is known about the mediating factors and the magnitude effect on contract design. However, power theories are by no means universally accepted. Critics maintain that while power can be useful in explaining

contractual problems in business relationships it should be seen as dysfunctional (Emerson, 1962; Pfefferr and Salancik, 1978; Cox et al., 2000, 2002). It is this dysfunctional aspect on the contract design in PPP that we will be exploring in the rest of the study

### **3.3 A Model for PPP Balance.**

Revisiting power Lonsdale arguments, the first element in Lonsdale's argument was that pre-contractual power relations will affect the ability of public sector bodies to negotiate post-contractual balance in PPP arrangements. The argument here is three-fold. First, power relations do exist in pre-contractual negotiations. Second, suppliers seek to use bargaining advantages for commercial gain, even at the expense of efficiency. Third, in the PPP context, this means unbalanced contractual arrangements, with little risk transferred, much of that returned during the contract period and giving unsatisfactory value for money, especially where there are significant variations. The latter are a problem, as they are negotiated over by a dominant supplier which is major threat to contractual balance. However, even when there is equal pre-contractual bargaining strength, risk remains if the buyer's bargaining team does not match the competence of the supplier's team.

While the Lonsdale risk transfer model has contributed to the debate on PPP performance by taking a different perspective, questions about its generalizability remained limited. His conclusion is based on two case studies in the UK and he did not say its findings apply to developing countries as well. For example, in arriving in his conclusions Lonsdale did not consider the implication of his study in a country like Ghana where PPP policy is being experimented for the first time. Moreover, his work called for more research to provide more

understanding of the issues he raised in his study from different environmental perspective. Some writers Utting and Zammit (2006) working at the United Nations have also added their voice for more robust studies on PPP particularly in developing countries so as to provide useful insight to make practical conclusions for public policy. Until now little is known about the conditions that influence pre-contractual bargaining power to either create power between buyer-supplier. Specifically, little is known about the way in which power from endowment resources impact on the dependent relationship between the public sector and the service providers. Based on the above limitations in our understanding relating to business relationships it is critically, important to examine the factors of power and dependent position when a buyer and supplier enter into an exchange relationship.

It is noteworthy to point out this study focuses on pre-contractual power resources between the public sector and private sector looking at the power resources variables. Others have covered the contractual problem of asset specificity with sufficient studies to explain the contractual problems and its high transaction costs and would not be followed in this work. As a result, this thesis seeks to extend Lonsdale arguments to investigate this issue further to provide more understanding about the effect of power on the ability of the public sector authorities to achieve post contractual balance. We now look at the other factor of negotiation resources and capabilities which Lonsdale argued can lead to sub-optimal contract design.

### **3.3.1 Capability and Resource of the Buying Function**

In this section, we examine the other factor this thesis will be focusing on:-the asymmetrical resource and capability of the public sector vis-a-vis the private sector mentioned by Lonsdale. Central to the argument in his model on commercial resources and capabilities of the public sector negotiation team, is the idea ill-resourced public buying managers may contribute to the difficulties in achieving a balance with the private sector. He contended that the private sector possesses superior negotiation resources and that gives it the ability to outplay the public sector negotiation team in a context of contract design.

This is in sharp contrast with Williamson's assumptions about buyers and suppliers as operating in business markets. Williamson assumes that buying and sales managers in business transactions are equally knowledgeable and well-informed and have the ability to select choices to arrive at efficient outcomes (Williamson, 1995, p. 39). However, these assumptions were contested by Lonsdale (2005b) in his risk transfer model, who argued that asymmetry in resources and capabilities in buyer-supplier relationships may sometimes exist and that this may allow either the buyer or the supplier to gain advantage in the pre-contractual negotiations. Even in cases where there is symmetry, he argued fundamental differences may still exist in terms of knowledge or experience. He supported his conclusion with cited cases in UK healthcare sector.

It is important to acknowledge that Lonsdale is not the only writer in this observation. Other studies have also raised concerns about the gap between the negotiation ability of buyers and

suppliers that had allowed suppliers to out-stage buyers in contract negotiation resulting in poor contracting signing poor contracts (Industrial Society, 2000; NAO, 2003c). Some writers (for example, Prahalad and Hamel, 1990) have observed that knowledge asymmetries exist because of differences in organisation design, path dependency and human resource endowments.

It is evident from above that there is real concern about the asymmetries that exist between the buyer's negotiation team and the supplier's team. This concern has been echoed earlier on by some independent reports coming from UK. For example, the NAO and PAC have expressed concerned about poor contract signings in PPP projects and have singled out poor commercial skills and inexperience on the part of public sector buying managers as major causes. Evidence of poor contract signings in Police Service Airwave project, the Libra project, the London Underground PPP projects and many other ones are cited in UK audit reports. In all these cases, poor contract signings are generally attributed to buying managers difficulties in understanding of the technical requirements and project risks (see NAO, 2000b; 2002b; 2003b; 2004). In more recent times, the competence of UK public sector buyers has been called into question in the contract for a single database for offender management to harmonise operations across the HM Prison Service and the National Probation Service. In a PAC 2009 report, the chairman Edward Leigh expressed concern over 'senior managers' ability to deliver such a project'. He stated his frustration on the incompetency of public buying managers in handling procurement contracts by saying that 'there was not even a minimum level of competence in the planning and execution of the project' (PAC, 2009). The report went on to further recommend that the commercial skills of buying managers should be improved to the level of a standard required in negotiations.

In developing countries where few studies exist, Smith and Hanson (2003) found that technical incompetency was largely responsible for bad contract signing in the water projects in South Africa (see also Gilson Grimm, 2004).

All these anecdotal cases have demonstrated that buyers in general and public sector buyers in particular often find themselves being either not in sophistication against their sales opponents in negotiations. However, the big picture that emerges is that the public sector buying managers are often dominated and sometimes may be bullied by their competent sales and marketing opponents. Although suppliers are often seen as having superior negotiation resources and capabilities, it is important to emphasise that this is not always the case. There are documented cases that point to the fact that buying departments are not always weaker than the supplier's sales team. In some cases some organisations, the purchasing department is well resourced, so much so that they can have an advantage over the selling function of their suppliers. In the food industry, suppliers of farm products find themselves in a very weak bargaining position with highly trained buyers (Hingley, 2005). Similar arguments can be raised for supermarkets and some food retailers in the UK and US, such as Tesco, Wal-Mart and Morrison, could be mentioned to be more knowledgeable and capable, providing them with an advantage in their relationship with their suppliers.

In yet other cases, the TCE assumption of well-resourced equivalence appears to be actually fulfilled. For example, the aerospace and automotive industries represent examples where buyers seem to enjoy similar resource and capability to those of their suppliers. Although it could be argued that some firms or the supermarkets use their economic power to bully vulnerable small suppliers to accept less than third rightful share of the gains little is known



about other factors that allow suppliers to gain pre-bargaining advantage outside the supply chain such as the public sector. Lonsdale, 2005a, 2005b) described areas such as training, professional qualifications, professional turnover as some of the problems militating against public procurement departments. By contrast, he noted that the sales and marketing department of the public sector are well-resourced in terms of training, and retention of professionals gives them an advantage in planning negotiation strategies. Until recently little is known about what conditions which may empower or disable a buyer and by extension the public sector managers to negotiate with suppliers at an equal competent level. Lonsdale study of UK public sector could be seen as drawing attention to the importance of public sector raising a well-resourced and competent negotiation team. Unfortunately, Lonsdale study did not specify what kind of attributes a good negotiator should possess that the public sector lags behind. Additionally, although, his work is useful in drawing a distinction between the procurement department and sales department in the context of procurement negotiations, they are descriptive and broad for operationalisation purposes. As a result, we turn to the literature to review what it says strictly staying within the confines qualities-competence team should possess and the capacity of deployment in the field of commercial negotiation. Issues like negotiation planning and detail negotiations are beyond this study.

### **3.3.2 Importance of Negotiation Resource and Capability**

The negotiation process has become a more important strategic tool in buyer-supplier negotiation as companies look to reduce their expenditure but increased product or service offerings. The literature points out the goal conflict between buyers and suppliers are reflected in attitudes towards risk and cost. Since profit is a function of revenue over cost of

executing the project, suppliers have strong incentives to use the negotiation process to maximise their returns and not pass value over to the buyer (Cox et al., 2003). With this objective in mind it is reasonable to expect that suppliers would adopt two-prong strategies; firstly, to negotiate for better price and secondly, to formulate terms to perform minimum possible under the contract to reduce cost. In order to be successful suppliers have to be present a strong negotiation team.

The implication flowing from above is that negotiation process has become a strategic tool for a supplier and the purchasing professionals working in the public sector have to negotiate increasingly better to obtain the best price with suppliers. This need for improved performance has been stressed by some writers such as Ahadzi and Bowles (2004). Studies in the IT sector suggest that suppliers continuously adopt evolving strategies to dominate the negotiation proceedings (see Lacity et al., 2009). Reilly (1994) on the other hand, found that a supplier's negotiation team does not eagerly show their hand in negotiation unless they are forced to do so through hard bargaining from buyers

From above discussions the importance of buyer's raising a well prepared and resourced negotiation team as their supplier's counterpart resonates in the bargaining literature. We can therefore expect that a well-resourced and capable negotiation team can achieve the best deal possible from any commercial deals. However, the difficulty lies in determining the attributes of a good negotiator. In the next section we examine the unique attributes that purport to offer negotiation advantage.

### **3.3.3 Attributes of a Good Negotiator**

The importance of a buyer raising competent negotiation team to achieve negotiation advantage with suppliers' marketing team has received less attention in the literature although few studies started looking at the problem. Many writers have drawn a link between efficient contract design and competence of negotiators and this has been duly discussed in the literature (Karass, 1994; Sturges, 2008; Lacity et al., 2009).

In a major study, Karass (1994) conducted a survey placing emphasis on analytical skills. The survey found that the source of negotiators strength comes from discrete knowledge such as industry knowledge, commercial skills, and knowledge in law and accountancy and suppliers markets. The survey also summarised the major indicators of a value-oriented negotiator as experience, education and analytical skills. He conceded that the negotiator's ability to perceive and exploit power – i.e. identification of risk and attitude to risk – are critical factors to successful negotiation and this may be difficult for negotiators with limited knowledge and understanding of commercial of risk in a particular industry. However, McDonald (1999) found that imbalance in technological skills results in significant disequilibrium that favours the supplier. Interestingly, these attributes are what the sales and marketing teams develop effectively for competitive advantage (see Ahadzi and Bowles, 2004; Mayer and Solomon, 2006; NAO, 2007).

The question of technical competence is recently raised by Lacity et al. (2009). The writers found that firms' success in negotiation was greater when buyers have technical knowledge about the transaction in IT contracting. They argued that this allows an organisation to

effectively bid, select, and negotiate an effective contract with a supplier to maximise value from its offering.

One key negotiation resource that is conspicuously missing in Lonsdale's analysis is market intelligence. Market intelligence has long been used by marketers to gather critical information about buyers' strengths and weaknesses, including issues on value of a particular transaction to their operational needs. As pointed out in the marketing literature, intelligence offers a competitive bargaining advantage. With the right intelligence about suppliers' needs, a buyer can gauge the scope of the supplier's key strength and vulnerabilities concerning the transaction and use the knowledge to build coherent bargaining strategy that will be at the level of suppliers' proposals (Baiman and Rajan, 2002; Ahadzi and Bowles, 2004).

The advantage to the public sector based on Lacity et al., (2009) studies is that buying managers may be able to develop proactive negotiation strategies to counter the domination strategies suppliers are likely to bring up. A further advantage is that the negotiators will avoid making costly errors of judgement when signing contract. This is significant as UK PAC on number of PPP contracts commented that failure to sign good contracts as a result of wrong judgement are attributed to insufficient for planning the negotiation strategy (PAC, 2009; Industrial Society, 2000; NAO, 2003c). It can be argued also that improvement in the resourcing the procurement departments and staff training may minimise the risk of being outplayed by more profit-oriented private sector sales and marketing teams

However, the consequences of poor bargaining skills on the part of buyers are that of increasing risk of hold-ups in PPP. Williamson (1985) also points to inefficient bargaining

post-contractually as one of the transaction failures in contracting. Although Williamson used inefficient bargaining in a different sense to refer to problems associated with post-contractual negotiations when there is a lock-in, it can also be demonstrated that inefficient bargaining at the pre-contractual stage could equally enhance hold-ups if the risk is not spotted before the contract is signed. As already noted, in contract regime, written terms are legally enforceable and the courts cannot be relied upon to reconstruct new meanings to fill gaps on behalf of a party to a contract (Williamson, 1979). In other words, the courts do not reward incompetent contracting. Based on this problem, one can reasonably see the possibilities of suppliers taking advantage of incomplete buying team, though this may not be the case.

The implication is that the responsibility of designing efficient contracts to protect the firm against risk of hold-ups is the negotiation team. On the other hand, a buyer negotiation team with full knowledge and skilful in negotiation, may lead to a possibility of taking the contract towards contractual efficiency. The assumption derived from above is that competent negotiators know at least, how to plan, manage hostile negotiation environment, to persuade their buyer counterparts and how to recognise and use power to their advantage.

The problem though, is that buyer's negotiations may be affected by lack of negotiation strategies when both incentive and transaction constraints of power are taken into account. From this perspective, the problem of avoiding legitimising hold-ups in the contract hinges on competency of buying managers, or who undertake negotiation on behalf of the public sector body. As Sturgess, (2008) argued negotiators' core attributes of a negotiation underlie the concept of power between opposing buying team and supplier's team. On the buyer side,

this will mean negotiators will surrender a degree of power to their supplier counterparts and concede on issues that would have been avoided

An important point that needed to be pointed out is that given the problem of catching up with the suppliers' sales and marketing team does not suggest that nothing is being done to build the capacity of public sector buyers. On the contrary, it is just that the problem of catching up with the suppliers' competence is far deeper than what is in the literature. The shocking revelation from NAO and PAC reports about the asymmetry of negotiation resources and capabilities of the UK public sector procurement managers prompted national capacity building and programmes to improve negotiation competency. Experience in UK suggests that various intervention programmes including training, recruitment of professionals and have not yielded the required results.

Others options have been explored to raise the standards of public buyer competency level of public buyers. One such short-term approach is the use of consultants by the government with two-fold aim. Firstly, to use the consultants to minimise the incidents of public sector buying managers being over played and secondly, to train procurement managers in world class negotiations.

All the above strategies are meant to empower the public sector buyers. However, this experiment was found not only to be ineffective but costly to the taxpayer. One particular drawback of using outside consultant highlighted by the chairman of PAC (2009) is that public buying managers take advantage of the presence of consultant to avoid taking

responsibility for poor project negotiations. In a recently released report on management consultancy fees, the UK NHS alone spent £478m on management consultants between 2005 and 2010, yet it was found that the consultants still could not save the health sector from being outplayed by suppliers (The Daily Mail, 2010; PAC, 2010). Moreover, in the same report the PAC (2010) expressed concern about their impact of the consultants on the negotiation capability of the public sector officials and the 'loss of commercial knowledge when the advisers leave' suggesting that the public sector may not have benefited from the consultants presence. Where this does leaves the public sector? It demonstrates the difficulties of public managers of catching up with suppliers. Although it is tempting to place the problem on poor bargaining strategies, what is not clear is whether the public sector may ever catch up with their opponents and negotiate contract at equally competent level given all the constraints buying managers face.

The problem is compounded because empirical research in this particular area finding causes and its impact on the efficient contract design and the appropriate contractual extra-safeguards against risk (i.e. hold-ups) are limited. It could also be the case that public sector buyers have resources and capabilities as the supplier's sales team, at least to improve outcomes at the negotiation table; they may lack the ability to transform the resources into powerful negotiation strategy. Further research is needed to provide the answer to this conundrum facing public buyers. In order to fill the gap, we have defined the negotiation competence in terms of unique attributes of commercial skills, experience and capabilities as the resources required to plan a powerful negotiation strategy for an advantage.

From the above, it can be concluded that the literature emphasises the importance of the need of the public sector to raise a well-resourced and capable negotiation team to match that of

the private sector- a mismatch likely to produce signing bad value for money. Given that the UK public sector with all its vast resources are still struggling to have its negotiation resourced to match that of the private sector it is reasonable to expect that gap between the public sector in Ghana and the more experienced private sector to be wider. However, little is known about the issue at this stage.

### **3.3.4 Supplier Performance**

Although the preceding discussions in this chapter and previous chapters indicate that the contractual problems of PPP facing public sector managers principally deal with hold-ups and challenges to implement mechanisms to achieve balance. However, it is not an end in itself, rather the approach is aimed at securing good value from suppliers. If we consider this aim as fundamental then we can reasonably posit that supplier performance is critical. This takes us back to power. Of the various factors that the literature discusses which support supplier performance, is when the buyer is mutually inter-dependent relation or a more preferably in dominance and the supplier is the dependent party. The reason as suggested by the power models is that supplier performance partly depends on the capacity of the buyer to choose the most optimal contract design and sufficient power resources to control the behaviour of suppliers in the relation (Cox et al., 2001). This implies that when the buyer enjoys favourable post-contractual balance may enhance its prospects to force suppliers to perform according to agreed minimum performance standards. From the economic perspective, TCE's approach to efficiency outcomes suggests that transaction cost is minimised when there is relationship alignment suggesting power balance (Williamson, 1985, 1991).



In the situation of buyer's dependency on supplier resources we noted in power theories could opportunities for the supplier to exploit the power relation to renegotiate the terms of the contract, and possibly reduce performance levels of the minimum delivery required. In a dependency position, the buyer has few opportunities to leverage value from the supplier (Cox et al., 2000, 2004). In other words, we can expect that the supplier in dominance will not pass on cost savings from the relation to the buyer. This of course will depend on other considerations of whether the supplier will recognise its bargaining leverage advantage and exploiting it and secondly, whether the buyer's negotiation team is able to design efficient incentive contract with extra-safeguards to neutralise the effect of supplier dominance.

An alternative scenario is that, if the buyer is in dominance the supplier may be forced to pass all cost savings to the buying organisation. Studies also show that firms that fail to achieve mutual interdependence suffer from poorer outcomes than those in properly balance relationships with suppliers (Masten, Meehan and Snyder, 1991; Silverman, Nickerson and Freeman, 1997; Mayer, 2000; Ménard and Saussier, 2002). In putting all that has been reviewed so far in this study, we arrive at a proposition that an adverse pre-contractual power relations may lead to post-contractual imbalance and this in turn put the supplier in dominance position. From this premises and we can expect poor performance from suppliers. This is the proposition that this thesis is going to explore in the empirical chapters.

### **3.4 CONCLUSION**

The preceding section reviewed Lonsdale three risks factor of pre-contractual power, asymmetry in resource and capability in negotiation. We have considered and extended his argument to identify some gaps in the literature that requires further research. Based on the literature reviewed and based on our research objectives we would be building evidence that may provide more understanding for public policy. In the next chapter we develop our hypothesis for the research.

## **CHAPTER 4**

### **Theoretical Model and Hypothesis**

#### **4.1 Towards the Analytical Framework and Hypotheses**

Chapter I discussed the importance of PPP in national infrastructure development and service delivery. The problem of risk transfer was discussed in Chapter 2 and we noted that empirical study results showed inconsistency results. We reviewed TCE theory on its framework for developing a balance in bilateral governance using credible commitments. The critique of the Williamson's credible commitments was taken in Chapter 3 alongside Lonsdale's argument that the public sector is not likely to develop post-contractual balance as a result of adverse pre-contractual power relations, asymmetry in resources and capabilities in contract negotiation. This chapter is structured as follows. Section 4.2 outlines the research problem and in section 4.3 provides the justification for the choice of research setting in Ghana using the two PPP cases. The result of the research hypotheses and summary of the chapter are found in sections 4.4.

#### **4.2 Problem Statement**

There is considerable amount of literature on the subject of bilateral contracting that discusses the problem of misalignments and risk transfer to the private sector. Empirical studies, using TCE models have investigated lock-ins and misalignments in PPP focusing on

asymmetrical investment in asset specificity and the problem of achieving functionality in the least cost economising way.

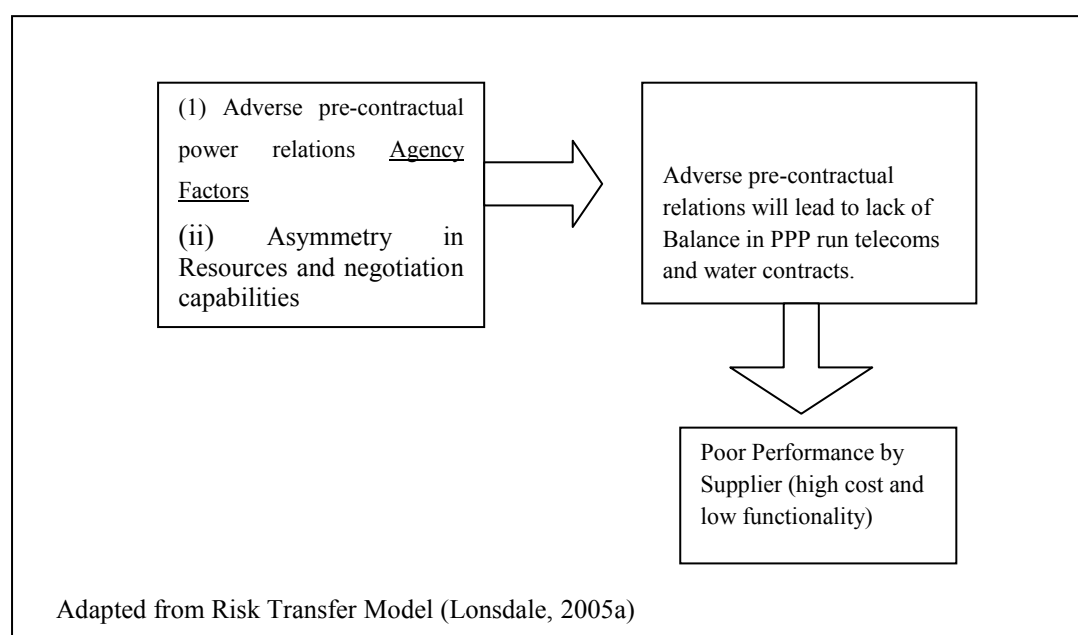
From the earlier analysis, it seems that endowment resources of parties to a transaction play a significant role in developing pre-contractual power relations, which in turn defines power balance and outcomes. Therefore the relative power position of buyers and suppliers are factors expected to influence the conditions that create balance within a given relationship.

In adopting the power approach to the analysis of the ability of the Ghanaian public authorities to achieve post-contractual balance and good supplier performance, in the implementation of the PPP policy in public provision, one is interested in the nature of internal and external factors that may facilitate or impede these efforts. Although some few studies have addressed the question of contractual imbalance in PPP relationship and its profound impact on supplier performance only few has considered it from pre-contractual power perspective (see Cox e al, 2001). In particular, with the exception of Lonsdale work fewer studies have investigated why it is difficult to successful apply Williamson credible commitments model to balance risk and minimise uncertainty in a relation. However, little is known about the conditions that impact on the ability of the buyer to develop a balance using TCE guidelines and with specific reference to Ghana, an empirical research on the impact of pre-contractual adverse power relations on Ghanaian public authorities is yet to be done. On the other hand, Lonsdale conclusions may not necessarily apply to Ghanaian context. The review of the literature suggests that developing countries like Ghana operates in a different political and economic environment and Lonsdale conclusions might yield different outcomes. More specifically, there is little evidence that to the best of knowledge of the author such a research has taken place in a developing country. It is therefore important that we examine

the factors that may impede the efforts of the Ghanaian public sector to develop post-contractual balance with the private sector and to achieve good performance.

The goal of this study is to empirically test two hypotheses that are deduced from the literature on resources endowment and dependency. To facilitate this we therefore frame the research question based on the preceding reviews taking into consideration the context of Ghanaian contracting environment with emphasis on pre-contractual relation. This allowed us to develop a model to examine Lonsdale arguments and also to explore new aspects of impediments to balanced bilateral contracting from developing country perspective. The model developed in Figure 4.1 allows us to address Lonsdale critique of TCE framework.

**Figure 4.1 The Theoretical Model for the Research**



The central question of the two case studies, therefore, is this: ‘Does the Ghanaian public sector have the ability to develop post-contractual power balance and achieve good

performance outcomes? In order to answer the question, the researcher aims to analyse the pre-contractual power resource endowments of the Ghanaian public sector and its private sector partners as the first independent variable and the second independent variable of negotiation resources and capabilities. To simplify the research process this study breaks it into the following sub-questions:

- (1) Is there a power relations structure arising from endowment resources of each the public sector (buyer) and private sector (supplier) and what their effect on balance contract design?
- (2) What are the effects of asymmetry in negotiation resources and capabilities on designing balance terms in the contract?
- (3) If the public sector authorities fail to achieve post-contractual balance can adverse pre-contractual power relations and negotiation resources and capabilities asymmetry explain that?
- (4) If the supplier failed to achieve the minimum requirements can the adverse post-contractual balance explain that?

By addressing these questions, the studies also address their broader implication for future PPP practice in Ghana with emphasis on the role of the World Bank as the major sponsor of the PPP initiatives in the country.

### **4.3 Justification of Ghana Choice**

Ghana provides a good case country for examining the introduction of PPP management contracts from a developing country context. Its selection for the study is justified by the following reasons. The concept and practice of PPP in Ghana is relatively new, although evidence indicates that there is a long tradition whereby the state and the society have collaborated at the community level to manage sanitation, refuse collection and maintenance of public toilets (Gibbon, 2002; Post et al., 2003; Cook and Aryee, 2006; Londero, 2009). Since the two PPP projects are first of its kind, one can reasonably expect implementation problems. The study will help policy makers to understand the challenges involved in the area of achieving balance and good supplier performance.

As it has been noted, the Ghanaian government has been in control of the two utilities for several decades but due to political interferences, mismanagement and waste had failed to provide efficient services. In an effort to provide a sustainable financial and managerial reforms in the two companies brought in the World Bank with its market reforms via the PPP route. A persuasive argument advanced by the World Bank was that the Ghanaian government will be able to gain more from the private sector through improved services and cost savings than it was then achieving (McIntosh, 2003; Kirkpatrick and Parker, 2004).

The implementation of the PPP model in these two utility companies has been characterised by domestic agitation and protests. At the heart of the opposition is the concern that the two management contracts were structured to favour the private sector provider and that technical issues were over-emphasised as against national interests of protection against commercial

protection is ignored (ISODEC, 2001; Green, 2003). Some reports (see Tearfund and Water Aid, 2003; CCOD Peace Report, 2005) argued that the implementation of market reforms in the utility sectors was undertaken without sufficient debate, and questioned the World Bank claims that the private sector, in managing these utilities, could deliver services efficiently. The study offers us a unique opportunity to obtain empirical evidence as to whether this new way of using the private sector to manage public utilities in the country has been beneficial to the country and what lessons that could be drawn. Although the adoption of PPP in developing countries and Ghana in particular is a welcomed idea, there is a need for empirical study to examine whether effective institutional structures are in place to secure the delivery of cost savings and benefits from the private sector to the public sector.

Finally, Ghana is also chosen to study the issue of post-contractual balance because, like all other democratic countries, public projects are public information and World Bank projects are also in the public domain which makes it relative easy to access key information on the two contracts.

#### **4.4 Hypothesis and Rationale for the Study**

On the basis of the literature review, we identify PPP has the potential to transfer risk to the private sector to achieve value for money for the public sector in functionality delivery in the most cost effective way. However, given the resemblance of PPP to bilateral governance of TCE, the implementation of PPP policy is expected to be beset with risk of hold-ups and supplier opportunism that could lead to loss of potential benefits possible from partnership.



However, TCE provides a credible commitment model for buying organisations as an effective mechanism to prevent hold-ups through equitable share of transaction specific assets or, if that is not practicable, posting of appropriate financial bonds. However, empirical results show that successful application of Williamson logic is not universal. While other studies found empirical support for contractual balance others did not (Bigelow 2001; Parker and Hartley, 2003; Nickerson and Silverman 2003; Lonsdale, 2005a).

The mixed results from the literature reviewed imply that there might be some unexplained factors responsible for the mixed results when asset specificity explanatory variable is held constant. With few exemptions (eg Cox et al, 2001; Lonsdale 2005a; 2005b; Sanderson, 2004), critical factors impacting on the ability of public sector managers to develop a balance using TCE guidelines have not been widely addressed. This is a clear omission in Williamson's assumption who had ignored power in his analysis. The aim of this study is to fill the gap in our understanding by investigating Lonsdale arguments that public sector buying managers will struggle to balance their relation because of its adverse pre-contractual power relations, asymmetry in resources and capabilities in contract negotiations using two PPP cases in Ghana. At this stage, and consistent with what has been discussed so far, the author now proceeds to test the following propositions.

### **Hypothesis One**

Adverse pre-contractual power relations, asymmetry in negotiating resources and capabilities, are likely to make it difficult for the Ghanaian public sector to achieve post-contractual power balance with the private sector as prescribed in transaction cost theory.

Most studies show that adverse post-contractual balance design impacts on the extent to which the public sector will achieve superior performance from suppliers. This is because the resource dependence relationship imposes limitations on the ability of the public sector to force the supplier to fulfil its pre-contractual promises, which in turn leads to poor supplier performance. However, the other consideration is that if the Ghanaian public sector was able to achieve a post-contractual balance, then it can be assumed that the public sector may be able to achieve good supplier performance. On that premises the second hypothesis is formulated.

## **Hypothesis Two**

H<sub>2</sub>: Lack of post-contractual balance would result in poor performance outcomes by the supplier.

## **Summary:**

In this chapter, the research problem and the two hypotheses were formulated while stating the rationale behind them. The author now proceeds to test these hypotheses. In the next chapter we develop a research design and data collection method to be used to study the Ghanaian PPP telecommunication and water contracts to test the proposition that the Ghanaian public authorities would not be able to balance their bilateral governance with the private sector service providers.

## **CHAPTER 5**

### **METHODOLOGY**

#### **5.1 Introduction**

This chapter discusses the research philosophy and research methods for the study and provides a justification for the choice of the research approach adopted by the author. The central proposition of this thesis is that the public sector may struggle to balance their relationship with the private sector. The thesis argument is that achieving a balance with the private sector under PPP is not straight forward matter as TCE prescribes in both the transaction cost theory and in PPP policy documents.

The research goal of this study is to investigate whether the Ghanaian public sector authorities have the ability to achieve post-contractual balance with the private sector. In order to answer the question this thesis is testing the primary hypothesis that adverse pre-contractual power relations, asymmetry in negotiating resources and capabilities, are likely to make it difficult for the Ghanaian public sector to achieve post-contractual power balance with the private sector as prescribed in transaction cost theory. The second hypothesis is lack of balance would result in poor performance outcomes by the supplier.

To achieve this objective, this chapter examines the different paradigms within which management research can be located, and then explores the different research designs and methods available. This leads us to consider the main research philosophical paradigms commonly found in social research. The chapter is organised as follows. First, the author

outlines the epistemological approach that underpins the study. This is followed by the research design and methods and the choice of a qualitative research design. The second section discusses the definitions and operationalisation of the key independent and dependent variables and measures. The final part discusses the actual evidence gathering and processing of data for eventual analysis.

### **5.2.1 Epistemological Approach to the Study**

The choice of methodology is influenced by the studies of ontology and epistemology. This entails the analysis of how research proceeds and the consideration of, for example, the kind of logic used in the generation and testing of theories and the criteria that must be considered knowledge. The tradition has been that researchers decide first the ontology and epistemology of any research, laying out the research assumptions (Rorty, 1979; Hammersley 1996; Smith, 1996) Ontology is concerned with researcher assumptions about the world view and what can be represented. Epistemology on the other hand is concerned with the nature, sources and limits of knowledge (Rorty, 1979; Smith, 1996). Broadly, there are three main core research philosophical assumptions in contemporary social research, identified as positivism, interpretivism and critical realism (Guba and Lincoln, 1998; Ratcliff, 2002).

In selecting the research philosophy for this study, positivist approach was chosen. In selecting the positivist approach, consideration is given to the objective of this research which is to test propositions concerning power and agency factors in Ghana with an attempt to uncover possible causal relationships to post-contractual imbalance and supplier performance. This suggests that alternative approaches like interpretivism and critical reality are inappropriate for this study for reasons to be discussed later. Positivism approach puts the

epistemological position of the researcher as one that assumes reality of the world is external objective (Hammersley 1996). From this view point, the researcher proceeds from the position that reality can only be understood through scientific analysis of a phenomenon being observed. Some writers (Berger and Luckmann (1966) contend that positivism orientation assumes that reality is external and objective and that the objective reality provides the foundation of human knowledge. The key strength of positivism as pointed out by Hammersley, (1996) was that positivist research has provided management with an ability to understand the ways in which organisations operate and be better able to predict and control their environments (see also Smith, 1983; Creswell.1994; Smith, 1996).

However, the other two competing paradigms of interpretivism and critical reality and other variant ones offer different world view of generating knowledge. For example, interpretivism is concerned with exploring the meanings of other people's action. In contrast to positivist assumptions, interpretivist views a reality as not external to the observer. From this view point the interpretivists argue that the social world can only be understood through direct participation and that knowledge is acquired through discovery from the perspective of the participants (Eisenhardt 1989; Guba and Lincoln, 1994).

However, both pure positivist and interpretivist approaches have been criticised by many writers (see Patton, 1990). Among others the key criticism of positivist paradigm is centred on its rigid structured design approach that imposes severe constraints on the researcher's ability to probe deeper for a fuller understanding of a social phenomenon (Morgan, 1998). Interpretivism on the other hand is criticised for being descriptive to generate theory to test (Smith 1996; Cresswell, 1994). As a result of the key weaknesses of the two paradigms,

Bhasker (1998) proposed critical realism to blend the two. Realism is the ontological position like positivism, recognises that external reality exists, and leaning on interprevism assumption insist that there are unobservable events that cause the observed ones and that knowledge can be acquired through discovery (critical realism) (Bhasker, 1998; Fleetwood and Ackroyd, 2004)

Although this study adopts a positivist approach, it also recognises that to properly understand power structure in PPP, it is important to seek in-depth understanding through probing and testing systems. Adopting this philosophy will help investigating the causal relation between individuals and agency, which is central to answering the research question of this thesis. The next section discusses the research approach, the techniques and procedures applied to the study.

### **5.2.2 Research Design**

This section discusses the research approach used in this study, the sources and methods of data collection, the limitations and problems encountered during the research. The key consideration that forms the basis for the data collection and analysis is derived from the research question of whether the Ghanaian public sector authorities have the ability to achieve post-contractual balance with the private sector. The research approach is framed by the results of the literature review that achieving a balance with the private sector is affected by power structure and the characteristics of the negotiation team affect the process and internal politics in the decision making process in procurement choice.

The goal of the study is to investigate and explain the impact of power on contractual design and not to make predictions. In line with the research objectives, the case study design is chosen, and the techniques for gathering data and generating evidence are mainly qualitative, using a semi-structured interview method. We discuss each in turn in subsequent relevant sections. Our discussions start with case study design.

### **5.2.3 Case Study**

The main consideration that confronts a management researcher is which research design to choose- sampling, experimental or case study- that best answer the research question (Patton, 1987; Eisenhardt 1989). In choosing the case study, consideration is given to the aim of this thesis which is concerned with explanation, rather than prediction. The use of case study research helps provide a clear understanding of the phenomenon being studied, in this case the adverse pre-contractual power relations and asymmetry in resources and negotiation capabilities of the public sector and their effect on the contract design. This research aims requires greater attention to in-depth research and deep probing. In this sense, the case study excels in comparison to either experimental or survey designs. In the case of the experimental design, its inappropriateness in relation to this study lies in the fact that the researcher has no control over the behaviour of the individuals and their motivation concerning the management of the two contracts and therefore there is no means of manipulating the officials involved in order to arrive at results as is normally done in a laboratory setting. In similar reasoning, the survey approach was not suitable for this study. The sampling approach, although suitable for large populations, is not appropriate in this study because they do not move beyond snapshots of ‘what ‘ or ‘how many’ questions to probe the ‘how and ‘why’ questions that are required in this case to provide deep and rich understanding of a

functional problem in public sector management and post-contractual balance. Moreover, the sampling approach is appropriate where the population is large enough and spread to support reasonable sample sizes and questionnaires (Miles and Huberman, 1984; Yin, 2003).

According to Yin (2003):

‘A case study is an empirical enquiry that investigates a contemporary phenomenon within its real life context, when the boundaries between a real life phenomenon and content are not clearly evident, and in which multiple sources of evidence are used.’

In the field of management studies, Yin (2003) noted that case study design provides an effective design for understanding and explaining causal links in real life interventions that are too complex or which cannot be played out in a controlled environment in order for survey or experimental research designs to be used (see also Punch, 2005). As it has been pointed out, a case research method in itself will not provide answers to the problems being investigated, but provides the phenomenon being investigated with a deeper and rich understanding of the social context in which the individuals involved in the two cases work and their level of understanding of the problems and possibilities of solutions (Scapens, 1990; Yin, 1993). In other words, since case studies provide ways of identifying management problems, it is considered as an important tool for management research in the Ghanaian case.

A further consideration after choosing a case study is whether to adopt a single or multiple case study design. A multiple case design is chosen instead of a single case with the aim to provide a more profound insight into problems affecting a balance contract that could provide a better understanding than single cases as recommended (Eisenhardt, 1989; Yin, 2003). One



option has been to select a perfect typical one from another African country but this idea was dropped when it became clear that negotiation access to conduct sensitive research on the issue of PPP in African studies, particularly for a non-citizen, was difficult.

The choice of research setting: the Ghana telecoms and GWCL partnership arrangements with the international suppliers reflects the significant problems of power relations and supplier performance given the uncertainties over World Bank conditions on its project financing loans and implication for PPP practice in Ghana. In addition, the selection criteria are primarily based on the ability of the two companies to contribute new insights to the constraints to PPP balance and the possibility of replication of the Lonsdale study in a different environmental context. Furthermore, the selection is guided by the reason that both cases offer a unique opportunity to contribute to both the theoretical and empirical strength of the study.

#### **5.2.4 Quantitative vs Qualitative**

This research, just as any other research in social science, was confronted with the choice between quantitative and qualitative methods of data collection and analysis. Researchers are often guided by the relative value of any of the approaches to their research objective. Whilst some researchers prefer quantitative methods to qualitative methods, as more scientific, objective and reliable, others hold the view that qualitative methods offer researchers an in-depth understanding of the phenomena being investigated (Morgan, 1998). Proponents of quantitative methods argue that the approach uses quantifiable and measurable variables by utilising statistical tools like mathematical models and graphs to draw a causal relationship of

what is being observed (Morgan, 1998; Denzin and Lincoln, 1994; Johnson and Duberley, 2000). However, the word 'qualitative', according to Guba and Lincoln (1994), connotes 'an emphasis on the quality of entities and of process and meanings that are not experimentally examined or measured in terms of quantity, amount, intensity or frequency. Despite the debate on the two techniques, the choice of one or both techniques, however, depends on the nature of the phenomena being investigated, the research objectives and the state of existing knowledge.

This research adopted qualitative study. The nature of the research topic does not make it easy to adopt quantitative approaches. This study is principally dealing with PPP policy implementation issue focusing on power constraints and capacity. In that sense, one needs to conduct an in-depth study into context and obtain greater understanding from the key stake holders and implementers to know their views and perception on specific issues of power and dependence. In addition, motivation of key actors, their behaviours, institutional and organisation and their stake holders are all factors needed to build a sample size to make the use of quantitative techniques feasible. This requires that key individuals and organisations involved in the implementation and management of the contract needed to be traced. Besides, the role of informants differed from one organisation to another and which made the design of a structured questionnaire for quantitative methods difficult and unreliable.

In view of the above reasons, the research used a combination of case study design and the qualitative techniques in data collection: semi-structured interviews, and documentary sources. Similar use of qualitative case study design have been used in the study of policy and implementation (for example, Ayee, 2001); supply chain management (Cox et al., 2002), PPP policy implementation (Lonsdale, 2005a). One important feature of these studies is that

they deal with phenomena that are complex and which involves many stakeholders, several actors and their behaviour in the process of implementation of strategies and policies. Under such circumstances, defining sample becomes difficult for quantitative approach to capture all the necessary motivation and the contextual explanations. This is because quantitative approaches mostly use close-ended questionnaires and the responses are restrictive, often leaving no room for further explanations (Miles and Huberman, 1984; Guba and Lincoln, 1989; Strauss and Corbin, 1990).

Despite these key strengths of a case study approach, critics contend it lacks academic rigour and results produced are not generalisable. However, measures have been adopted to minimise reliability and validity problems. Raimond (1993), for example, suggested that researchers should subject their work to a reliability test by asking the question: ‘will the evidence and my conclusion stand up to the closest scrutiny?’ The thesis followed the research tradition of linking the two hypotheses constructed from the literature review to provide guidance in planning the research and its execution. Care has also been taken to guide the reader through every stage in the research process to enable an independent assessment on how the researcher may have been influenced in arriving at the conclusions. Following Eisenhardt (1989) and Easterby-Smith et al. (2002) and others this thesis used different sources of evidence as a form of triangulation. Thus the virtue of the qualitative approach used for this study is that it allowed a combination of in-depth interviews with key informants, and use of variety of documents. The sources of information and methods of data collection are discussed later in the chapter. Meanwhile, the next sector discusses the operationalisation of the variables for the study.

### **5.3 Operational Definitions of Constructs**

A construct is a concept usually used to describe a characteristic or a property that underlines the measurement of a phenomenon (Mendoza and Prabhu, 2002). An indicator, on the other hand provides information about a variable to be measured. Indicators can be viewed as variables and can be used to measure the status or a condition of a phenomenon or process (Bell and Mores, 1999; Mendoza and Prabhu, 2002). This study uses indicators to assess the pre-contractual power relations and other variables as described by Lonsdale in the risk transfer model for PPP. Owing to the critical role that indicators play in measuring a phenomenon in a piece of qualitative research, a set of indicators should be robust and holistic to allow abstract variables be broken down into their constituent elements which in turn can lend themselves to formal analysis (Bell and Mores, 1999; Mendoza and Prabhu, 2002).

#### **5.3.1 Qualifying Variables**

The study used the qualifying variables (explained below) provided in the TCE framework. These are identified as asset specificity, uncertainty and switching cost in the TCE framework and underpins the TCE explanatory (variables). In a contract where there is no significant level of asset specificity, uncertainty, and switching costs, it is easier for the transacting partners to use market exchange. On the other hand, where these are present raises the possibility of risk hold-ups and supplier opportunism. These variables could frustrate any genuine attempts to build sustainable balance unless the appropriate incentive and sanction mechanism are designed to balance the risk and uncertainty in the relation.

Asset specificity is defined in the study as fixed assets and any relationship specific adaptations needed to support a relation. It is important during the research process to establish whether a relation qualifies as bilateral governance in terms of the criteria lay down in the TCE framework. If it is found that asset specificity, uncertainty and switching costs are trivial then the case does not merit this research attention. On the other hand, if these variables are significant, it validates the choice of the case for the research enquiry. However, this study considers asset specificity as a controlled variable. Firstly, the investments that had been made in the past or that would be made during the course of the project implementation were done as a normal necessity and not at the insistence of the suppliers. Secondly, although they are specialised assets there are not subject to diminution of value or write offs as they would continue to be used in the two companies' operations even if the contract terminates prematurely. Third the property rights control and ownership rests with the government which means all intellectual property that may arise from the collaboration belongs to the government and not a subject of conflictual negotiations. All the above reasons meant the issue of joint contribution to the dedicated assets, although important consideration in the two cases, their impact on hold-up of Ghana government in the relation is minimal. The added advantage to this research agenda is that by controlling assets specificity, it would be possible for us to isolate other factors that have the potential to create lock-in effects for the government.

Switching cost refers to the cost of transferring from one supplier to another and includes costs of: (i) Searching the market again; (2) re-negotiation costs; and (3) bringing the new supplier up to a satisfactory level. If the cost of switching is higher for the buyer than for the supplier, a shift of power balance to the supplier occurs.

In the context of this study, *uncertainty* refers to prevailing conditions that arise in the course of contract performance that were not anticipated or foreseen at the time the contract was signed and as a result of which parties would have to make costly adjustments. This includes tariff increases, regulations and the unpredictable strategic behaviour of partners in relation to post-contractual opportunism.

### **5.3.2 Definitions and Operationalisation of Concepts**

This section focuses on the review of the key concepts which supports the two hypotheses. Both the dependent variables and independent variables are defined and indicators to measure them are provided. Given the two hypotheses developed from the literature review two independent variables for the study are: pre-contractual power relations, negotiation resources and capabilities. These are operationalised in the subsequent sections.

### **5.3.3 Independent Variables**

The independent variables used in the testing of the first hypothesis are identified as follows:

- (a) Pre-contractual power balance
- (b) Balance of resource and capabilities between the negotiation teams

The pre-contractual power relation, following Cox et al. (2002) is defined in this study as the ax-ante power structure between a buyer and the supplier in a business exchange relationship.

Following the resource dependency model, power structure arises from resource endowment of parties in an exchange relation. There are utility, scarcity and uncertainty.

These variables are defined as follows:

Utility is used in the context of buyer-supplier relationship to refer to the importance of the resource to the other party's operations (Houston and Gassenheimer, 1987; Cox et al, 2000). In other words it is the measure of an individual satisfaction in any given outcome from an exchange. Target value is assumed in this thesis. It is the extent to which a buyer and a supplier hold in importance the resources the other party brings into the relation.

To the Ghanaian public sector, future utility of the supplier's offering is measured by the expected outcome in the fulfilment of its mandatory public and political obligations to the people. To the supplier its future utility is defined by the extent to which the transaction results in operation performance and commercial gain.

To fully understand the concept of utility, the relative degree between a buyer and a supplier in an exchange relation is distinguished along the indicators of the operational and commercial/strategic importance of the transaction to each party (see Cox et al., 2002; Sanderson, 2004; Lonsdale, 2005a). Figure 5.1 shows the framework for the specification measurement.

**Table 5.1 Framework for the Specification and Measurement of the Variables**

Core Concept	Key Dimensions	Key Indicators	Indices
Pre-Contractual Power	Buyer Dominance  Inter-dependent (Balanced)  Independence  Supplier Dominance	<u>Utility</u> Of the buyer resources: i.e. expenditure and prestige Supplier's resources: product or service offerings <u>Scarcity</u> Alternatives or substitutability of buyer's transaction or supplier's resources for the other party Political guarantees and commitments  <u>Information</u> Access to information on cost base and rate of returns. Verify claims made by the other party	Operational importance of the resource Commercial/strategic importance of the resource Ratio of transaction value to the supplier's overall turnover  Availability of the equivalent buyer or supplier's resources External pressure to take a particular course of action Urgency of the transaction  Cost base of suppliers  Project budget available .industrial benchmarks. suppliers
Resource and Capabilities	Degree of distribution of skills and technical knowledge (balanced and unbalanced)  Degree and type of intelligent interaction with opposing negotiation team (reactive to proactive)	Competency: skills in Commercial knowledge and communication skills in contract negotiations  Industry specific knowledge in private supplier operations  Negotiation Planning and Strategies	<u>Technical Background</u> Qualifications, training, number of Staff and recruitment experience Legal experience  <u>Technical Support</u> Frameworks and standardised contracting procedures and processes Permanent negotiation team in place
Post-contractual balance	Contract and governance design	Inter-dependent relation Contract terms and conditions. Extra-contractual governance features	Risk sharing Incentives and use of financial bonds Information sharing
Supplier Performance	Targets set for supplier to achieve over the contract period	Meeting the satisfaction of the public sector company	Achieving minimum performance required by the government. Evidence of passing cost savings to government.

The concept of the operational and commercial/strategic importance of a resource, product or service is defined below to provide more understanding for their measurement.



(a) Operational importance of a resource: This refers to the extent to which a particular resource, product or service is considered by either the buyer or supplier to be critical its day to day performance in fulfilling its mundane functions. From the supplier's perspective, a buyer's business is operationally important if the supplier depended on that transaction to serve its customer needs or markets. In the case of the public sector (i.e. buyer), the supplier's service is operationally important if the government depends on it to keep vital public services running. On the other hand, if the buyer or the supplier's business or services merely plays only a supportive or insignificant role in achieving its objectives, it has a low operational value.

(b) Commercial/Strategic Importance: The commercial importance of a good or service refers to its relative value in monetary terms to the supplier's overall revenue generating activities. If the ratio of the value of the buyer's expenditure (contract price) to the overall turnover of the supplier firm is high with no other business opportunities available in the market then the buyer's transaction is considered high. On the other hand, if the ratio of the business volume is low then in terms of commercial value, the transaction is measured as low. From the buyer's side, a supplier's service offering is considered high strategic importance when it forms the core function of public responsibility to meet its mandated responsibilities.

The second indicator in the pre-contractual power resources is Scarcity: This is defined as the degree of availability or non-availability of sources of a resource to meet a need outside the buyer-supplier relation. The degree of buyer's or supplier's scarcity is dependent on whether the buyer or supplier has alternative or substitutes for meeting their respective needs. Substitutes for the supplier market refer to the existence of products or services to those offered by the supplier in the industry.

Supplier Scarcity: supplier power: The degree of a supplier Scarcity to a buyer is measured by the degree of competition that the buyer can stimulate during the bidding process. If there are few suppliers in the market or when there are few or no alternatives or substitutes. These conditions when present in the supply market would make the buyer become dependent on the supplier for all of its needs, which, in turn, will affect its bargaining position with the supplier if that supplier has other buyers to do business with.

Conversely, if the supplier's product or service could easily be substituted with another one or alternative suppliers exist, the buyer's requirements could be procured from other available then the bargaining power of the supplier is diminished.

Buyer Scarcity:

The supplier faces buyer scarcity, if the supplier has no other business opportunity elsewhere outside the buyer's transaction. If the buyer is the dominant trading partner in terms of business volume and the supplier has no prospect of developing other business opportunities elsewhere then the buyer's scarcity is high. However, if there are other business opportunities besides the buyer's business, then the supplier faces low buyer scarcity. In both scenarios, bargaining power is determined by availability or non-availability of alternative sources of a resource. In combination, the proposition is that the more a transaction is to its operational or strategic needs, the more it is likely to be locked-into the supplier.

Information Asymmetry: This refers to the availability of critical information about a transaction that would enable the buyer and the supplier to verify each other's claims and

propositions. This study limits the information requirements to costs sheets, returns and operational requirements and efforts to complete the transaction.

This thesis takes the position as indicated in the literature (see Cox et al., 2000 and 2004) that when information about pricing and costs supplier's costs sheets or buyers value attached and what he is willing to pay for a resource who ever has private information and asymmetry has a bargaining advantage. If the buyer has limited information on a supplier's cost sheets and rate of returns, and the supplier has limited information of buyer's budget then there is no bargaining advantage to any of them, They either in independence or interdependence relation. On the other hand, if the buyer has limited information on suppliers level of efforts, cost sheets and rate of return and the supplier has information on buyer's budget for the project then the supplier has bargaining advantage over the buyer if the supplier's private information is not revealed. The reverse is true. If the supplier has limited information on the buyer's needs in the transaction and the buyer has full knowledge about the supplier's profit margins gives the buyer an advantage to challenge supplier's price proposals.

It is important to point out that the three variables of utility, scarcity and information are interact with each other, although relative critical resources and possibilities of relative availability outside are strong indicators of pre-contractual bargaining power (Emerson, 1962; Cox et al., 2001). If a resource or services required in an exchange is important to the buyer but not available outside the relation then the utility of the supplier's offerings to the buyer is high and the buyer becomes dependent on the supplier. This indicates supplier dominance in the relation. If the buyer's transaction is critical to the supplier's business and difficult to replace then the supplier's utility is high indicating dependence relation for the supplier. Similar reasoning applies to a situation where the buyer and the supplier utility is

similar and none has no other means to satisfy their needs outside have equal bargaining power inter-dependence relation). In the same way lack of information about the vulnerabilities of the other party may limit the ability to exercise its bargaining power and leverage. Thus, the degree to which all three pre-contractual power indicators together impact on the buyer and supplier provide the basis of their comparison and measurement of their relative power structure. As a sequence, the data gathered during the interview and documentary sources were used to construct and analyse the pre-contractual power structure according to the measurement framework presented in Table 5.2.

**Table 5.2 Framework to Determine the Pre-contractual Power Relation**

Contract power resources	Buyer	Supplier		Pre-contractual power structure
Utility	High	Low	The buyer is more dependent on supplier services	Supplier Dominant
Scarcity	High	Low		
Information	Low	High		
Utility	Low	High	The supplier is more dependent on the buyer's transaction	Buyer Dominant
Scarcity	Low	High		
Information	High	Low		
Utility	High	High	The transaction is of equal importance to the both the buyer and supplier.	Inter-dependent
Scarcity	High	High		
Information	Low	Low		
Utility	Low	Low	The transaction is of no importance to either the buyer or the supplier	Independence (i.e. a Each partner has power but independent of each other's power influence).
Scarcity	Low	Low		
Information	high	High		

Adapted from Cox et al, 2001

Pre-contractual power can be viewed alongside agency factors such as negotiation resources and capability, and internal politics. It is hypothesised in the risk transfer model that these two factors augment the pre-contractual power relation.

### **Negotiation Resources and Capabilities**

The pre-contractual negotiations is the most crucial process in negotiating better terms and incentives schemes to create balance in the contract design. The objective to operationalise negotiation resources and capabilities is to derive key indicators that will make it possible to measure the relative strength of the two negotiation teams from the public and the private sector bodies. We modify the model provided by Karass (1994) that of Lonsdale (2005a) to account for the differences from Ghanaian perspective.

The prior development of these 5 indicators from the literature defines the relative strength of each negotiation team. Negotiation resources are defined in this study as productive factors or the collective wealth of the negotiation team which creates negotiation advantage in pre-contractual negotiations.

The concept of resources is distinguished into competence and to measure the relative degree of ability between a buying negotiation team and the supplier team (Karass (1994; Lacity et al, 1996).

The factor ‘experience’ refers to previous engagement or familiarity with field knowledge in similar negotiations or over a period of years in actual practice which has resulted in superior understanding of the negotiations.

The commercial resources in negotiation are operationalised as follows:

**Skills:** refers to the ability and capacity acquired through deliberate adaptive efforts involving acquiring and understanding of knowledge (professional training) that enables an individual to undertake bargaining process successfully (Lacity et al, 2009). It is the ability to understand technical requirements of a transaction, market conditions and the use of analytical skills to make a choice that promotes organisation interests.

**Independence** refers to ability to apply objective and professional judgement in the negotiation without undue influence from political authority or any other authority outside the body with the requisite competence to make professional judgement.

**Deploying of Resources:** It is the ability to deploy resources and expertise the negotiation team needs in order to perform its core negotiation function relative to achieve the organisations objectives relative to the other party. This part is introduced to demonstrate the extent to which the bargaining resources are employed during contesting bargaining process to gain an advantage over the other party. It is assumed that both the buyer and supplier aimed at using the negotiation process to acquire control in the distribution of risk and value capture (Karass. 1994).

The following predictions are made concerning combination of the inequality between buyer's negotiation team and supplier's team.

- (1) The buyer will have poor deals if negotiation team is not in possession of these resources or/and not able to deploy them during the negotiation with the supplier's team.

(2) The buyer will not be ‘outplayed’ if its negotiation team is able to deploy the resources and capacities that matches or is superior to the supplier’s negotiation team. That also implies that if the buyer is in adverse pre-contractual power balance with the supplier, could still make the best out of the situation if it is well resourced relative to the supplier’s team capable of negotiating competently.

Similarly, if the supplier is able to deploy superior negotiation resources and capabilities then the supplier will outplay the buyer by getting the best out of the negotiation. The framework to measure the relative resources and capabilities are illustrated in Table 5.3 below.

**Table 5.3 Framework to Determine the Relative Resources and Capabilities in Negotiations**

Indicators	Buyer	Supplier		
Negotiation Resources			Ideal State	Relative State
Skills	High	High	Equally matched to engage in intelligent and professional negotiations	Symmetry
Experience	High	High		
Independence	High	High		
Training	high	high		
Skills	High	Low	Buyer is more positioned to make better contract judgement than the supplier	Buyer more competent (superiority)
Experience	High	Low		
Independence	High	Low		
Training	high	low		
Skills	Low	High	Supplier more positioned to make better contract judgement than the buyer	Supplier is more competent (supplier’s superiority)
Experience	Low	High		
Independence	Low	High		
Training	low	high		

Source: Adapted from Cox et al, 2001

The relative measurement is based on the assumption that, the wider gap the supplier negotiation team opens up between themselves and the buyer, the less prospects to create a level playing field for the buyer to negotiate on arm's-length basis.

#### **5.3.4 Dependent Variable**

In Chapter 3 and further developed in Chapter 4, the need for the public sector to develop a post-contractual balance with the private sector was underlined as a prerequisite for good supplier performance. A case was made, however, that the ability of the public sector to achieve post-contractual balance with the private sector may be made more difficult by an adverse pre-contractual power relation.

##### **5.3.4.1 Hypothesis 1: Dependent Variable: Post Contractual Balance**

In order to answer the research question of whether the Ghanaian public sector has the ability to achieve post-contractual balance with the private sector operators, we make the assumption that the public sector is seeking to balance its relation with the private sector, which in turn, provides opportunity to minimise transaction costs whilst maximising value for money in the transaction (Pollock et al., 2001; Grahame, 2003). The term 'post-contractual balance' is used in this study to mean that there is no domination of either the government as a contracting party or the supplier (Buchanan, 1992; Cox et al., 2000). In this sense both parties adopt a shared way of working together that allows each of them to achieve their minimum performance outcomes. Previous studies (Cox et al., 2002; 2004) and recent studies by Lonsdale (2005a) establish that post-contractual balance is achieved in a partnership when



there is no dominant partner in the relation to exercise control over the other. In this study, working arrangements is related to all deliberately induced administrative and governance structures) that support the equal allocation and distribution of risk and sharing of benefits in the relation. Contracts can be understood to be institutionalised and the administrative structures as those agreed arrangements that spell out the rights, obligations and expectations of the performance.

The indicators for post-contractual balance used as proxies in the study.

- i) Balance in the allocation of risks. If risk is equitably distributed by parties ie equal investment in assets or through the posting of financial bonds.
- ii) The contract design integrates the necessary incentive structures and self-enforcement agreements with necessary incentive structures.
- iii) Provisions available for exit/ contract reviews.
- iv) Access to information and regular submission of reports.

It is assumed that these indicators when present in the contract constitute a balance ie exhibits a fair representation that do not impose onerous obligations on one party and not the other. On the other hand, the relation will be unbalanced if these indicators favour the Ghanaian public sector or the supplier as the case may be.

#### **5.3.4.2 Hypothesis 2: Dependent Variable: Supplier Performance**

The research considers the issue of supplier performance in the second hypothesis. This study uses proxies to assess supplier performance (Skelcher, 2008). This thesis takes the view that buyers are usually satisfied if they receive the minimum functionality expected at the negotiated cost (Cox et al, 2004). From this premises, the targets set for the supplier in each case (ie installation of public facilities, extension of services, cost efficiency and service quality) represent the minimum functionality and the cost savings Ghana government expects from the private service providers to achieve. If these performance targets are achieved, it is presumed that the supplier has fulfilled its pre-contractual promises and to the satisfaction of Ghana government (public sector). On the other hand, if the minimum performance required is not received at the end of the contract then the government has failed to achieve good supplier performance. Using pre-agreed targets to measure a supplier's performance is widely used in qualitative research (Rouse and Hodge, 2006) and in buyer-supplier long term collaborative relationships (Cox et al, 2004). Moreover, the same methodology was applied to measure the performance of the earlier telecom contract between GT and TMP and is expected to be used by the government in the contract between GWCL and the AVRL (Amin, 2007; Ainuson, 2009). Additional proxy is used and that is related to the conduct of the supplier during the contract execution stage. The objective is to enable us measure whether or not the supplier took advantage of the power circumstances to hold up the Ghana government in the delivery of functionality and cost. In other words whether adverse post-contractual balance had an effect on the ability of the Ghana government to achieve minimum performance from the supplier or implicitly or explicitly engaged in acts that went against the contracting client, in this case the Ghana government.

#### **5.3.4.3 Measuring Instruments (Measures)**

Having defined the concepts of the independent and dependent variables, there is a need to create an appropriate instrument for data collection for the case study. The data for the two cases were collected using semi-structured question formats with the same questions for both the buyer and supplier. The research questions allowed relevant data to be collected from both the public and the private sector side. In the case of the suppliers, the research questions allowed data to be collected about their power resources endowment and to be compared and measured. Thus, the development towards post-contractual balance is linked with the relative pre-contractual power resources in the relationship. The questions were grouped according to their specific format and presented in different sections to measure each variable construct. A total of thirteen variables were measured in the present study with the objective of capturing the public sector's and supplier's perspective on the following:

- (i) Their respective pre-contractual power resources focusing on utility, scarcity and information.
- (ii) Their respective resource and capability in relation to the contract negotiation.
- (iii) The purpose was to identify both the public and private sector points of view and how they arrived at the point of view.

In relation to contract design, the objective is to:

- (i) Obtain the public sector's perspective on whether the contract was balanced.
- (ii) Obtain the supplier's perspective on whether the contract was balanced.
- (iii) Obtain the public sector's perspective on whether the service provider performed as expected.

(iv) Obtain the supplier's perspective on whether they performed as expected.

The purpose here is identifying why they hold that point of view and the basis for that, and in addition to find out how public sector dissatisfaction with the supplier's performance, if any, was handled and the view of the supplier on that issue.

Five of the variables were 'pre-contractual power variables' as they relate to the assessment of a pre-contractual power balance between the public sector and the private sector. Five variables were around resource and capability as they relate to the assessment of the relative negotiating strength of the GT and GWCL with their respective private sector service providers. Two variables were related to the internal politics as they relate to the degree to which decisions were taken to maximise private sector benefits from the relationship. Finally, two variables - one for the assessment of post-contractual balance and the other for the assessment of the supplier's performance are provided.

#### **5.4.1 Measures used in Part of the Semi-structured Interview**

The main aim of this section is to outline the design of the semi-structured interview question guide that allows data to be collected in a form that facilitates the assessment of power resources of the public sector (buyer) on one side against the assessment of the power resources of the private sector supplier.

The interview schedule is divided into six parts. Part A is related to general questions on personal information. Three of the questions contained in the interview schedule were more general to collect information on whether the transactions were characterised by qualifying

variables. Part B of the interview schedule measured the utility, scarcity and information variables. Seven of the questions measured the pre-contractual power relations. Part C of the question schedule measured the indicators of the resource and capability asymmetry. Eight of the questions measured the remaining variables of training, experience, qualification. Part D of the schedule measured the indicators of internal politics in decision-making in procurement.

Part E of the interview questions measured the post-contractual balance and Part F measured supplier performance.

All of these variables are described in (1a), (1b), (2a) and (2b) below.

#### **5.4.2 Measures used in the Interview Questions**

The researcher interviewed each representative of the buyer side, i.e. seven directly working with the two public sector companies, and six managers from the supply side.

Independent Variables: utility, scarcity and information

1a). The semi-structured questions were used to measure variables related to the assessment of pre-contractual relations in the relationship. The interviewees both from the buyers (i.e. the two public sector companies) and their suppliers were asked about the relative utility of the transaction to them (operational and strategic importance of the transaction to their business operations).

In relation to the measurement of the relative scarcity between the public sector and the private sector, questions were asked about the availability or otherwise of either the buyer's transactions to the supplier and about the degree of the availability of alternative suppliers of management services to the public sector.

The semi-structured questions measured the information variable by asking questions on the extent to which the relevant information about key areas of the transaction (i.e. cost, profit levels) were freely available to each of the parties.

1b) The independent variables: Resource and Capability Three questions contained in the interview measured the relative symmetry of resource and capability of the buyer and supplier negotiation teams by interviewing both the public sector and the private sector. Issues asked about included professional qualifications and the experience of each member of the negotiation team had in handling similar transactions in the past.

Other interested stakeholders - two government ministers and a World Bank country corporate affairs representative - were interviewed on areas pertaining to their particular role leading to the award and management of the contract. The questions focused on their impact on the ability of the public sector to develop a balanced contract.

**(2a) Dependent variables:**

The interview asked questions to establish the degree of contractual balance from the buyer and the supplier. Two questions were about how risk was shared between the buyer and the supplier.

## **(2b) Supplier performance**

The interview asked three questions in determining supplier's performance, asking what targets were set for the supplier to achieve at the end of their management tenure with the company. The aim of this part of three interviews was to establish whether the public sector thought that the supplier achieved the agreed performance targets.

In order to determine the actual performance of the service provider from both the buyer and the supplier, the researcher has to identify the clear targets and expectation of the public sector before the commencement of the contract.

The approach was to ask the public sector to identify the following.

- (i) Each of their needs, and their motivation for entering into the contract.
- (iii) The minimum requirements the private service provider is expected to achieve at the end of the contract period.
- (iv) Whether the service provider achieved this minimum performance and to the satisfaction of the Ghana government
- (v). Assess the impact of adverse post-contractual power on the impact of supplier performance and if service providers performance was below expectation, their opinions on their performance.
- (v). How does the Ghanaian public sector company assess the performance of the private sector in terms of the key criteria set in the contract?

Items (i) and (ii) sets capture what the public sector expects from the contract. Items (iii) and (v) provide the means of assessing the supplier performance. Item (iv) captures the supplier's

perspective on its performance and explanations. This is necessary because the service provider may have its own interpretation of performance, and about factors that may have impacted negatively on its performance.

Other supporting performance information was obtained from GT and GWCL published reports, supplier websites and press releases from the government sources.

#### **5.4.3 Procedures for Interview Data Collection.**

This section describes how the semi-structured interview schedule was developed and tested for the study. It also describes the format that was used to collect the data using semi-structured interview questions.

Based on the conceptual framework, derived from previous works (Cox et al., 2000; Lonsdale, 2005a) a list of indicators also derived from previous works was chosen to measure the variables. As a consequence, the interview questions were developed to measure the variables operationalised so that evidence from the data obtained would allow for conclusions to be drawn as to whether the two hypotheses were supported. The use of semi-structured interviewing is a powerful method of data collection and is preferred by many management researchers. It allows the researcher to collect the perceptions and experiences of informants (Hoepfl, 1997). Miles and Huberman (1994) observed that interviews provide opportunities for investigators to ask for further clarification of responses and also for the respondents to seek further explanation of the questions asked.



However, as stated by Saunders et al. (2007), the first draft of an interview schedule is never perfect. This can be problematic when interviewing informants to capture perceptions and judgements from senior managers. For example, Saunders et al. (2007) pointed out that managers are more likely to respond to what is supposed to be done and not what is actually done. This increases the danger of bias being introduced into the interview that will seriously impact on the reliability of the evidence gathered (Scapens, 1990). This requires that the data collection instrument should be tested to establish that the responses obtained would be appropriate for the measurement of the variables. In this case the questionnaires were tested in a pilot study as this would provide valuable information to make the necessary changes in the questionnaires and to eliminate potential biases. A pilot study was conducted in this study and is now explained.

#### **5.4.4 Pilot Study**

A pilot study of the questions was conducted on the water company and the telecom company for two reasons. First, the purpose was to introduce the research project to the potential informants and to ensure that all misconceptions about the research were cleared for the purpose of data collection. Second, the interviews were carried out to explain the concepts and their meanings and to gather initial information about how the potential respondents understood them. All the interviews were less formal, allowing free discussions about their understanding of the research areas. The pilot included the following steps. First, a letter of introduction was sent to the managing director of GWCL explaining the purpose of the research. Four managers from GWCL and GT on the buy side and two representatives from the supply side were interviewed. Three of the answers obtained revealed potential difficulties for the respondents, particularly with the questions directed towards the functional

managers on political questions. The pilot phase helped in the identification of the performance metrics criteria that reflected both the public and private sector perspectives. They believed that assessing supplier performance based on the targets set in the contract fairly reflected performance assessment. The information was used in designing the questions to reflect that perspective. The main problems included the following:

- (a) The respondents on the public side were reluctant to answer questions related to financial data and the political nature of the contract, partly because of their sensitive nature and partly because of the official secrecy oath taken by the public sector managers.
- (b) The information requested on absolute hard figures was deemed as time difficult by respondents because most data had been sent to the archives or destroyed.
- (c) Details of procurement staff strengths and actual qualifications were considered sensitive to make public.

Feedback from the pilot study was used to produce the final version of the questions (see Appendix A). For example, regarding items (a) and (b) instead of asking direct questions and demanding copies of the financial information, the questions were designed broadly to capture their views about how the organisation has performed in terms of their finances.

In relation to item (c) the questions were redesigned to capture broadly their views about professional background, training and experience of the procurement staff and about the negotiation team that represented the company vis-a-vis the private sector team. This

approach worked well as the relevant evidence was successfully teased out of the responses from the interviewees to build a clear picture of the financial situation and the degree of differences in their resources and capabilities with the private sector. At the end of the interview process, the researcher was able to establish the relative staff strengths and broad qualifications of the procurement staff and their training needs that made it easier to compare them with the service provider.

The pilot study also brought out the importance of designing specific questions to capture the views of the World Bank and another set of questions to obtain the views of the two government officials interviewed.

In summary, Table 5.4 below shows the detail research method used in the entire research.

**Table 5.4 Approaches to Data Collection and Analysis**

Phases	Strategy	Instrument	Analysis and Findings
1	Pilot	Semi-structured interview	
2	Qualitative: Interview	Semi –structured (Appendix A)	Recording, transcription and coding the themes in relation to the variables
2b	Collection of documentary evidence		Public sector findings documented Private sector findings documented Integrate both results into the third phase of data analysis
3	Results and Conclusions	Qualitative analysis	Findings Compared Public companies and their private sector suppliers

#### **5.4.5 Sources and Evidence: Selecting Interviews**

This section describes how the companies involved in the Ghana telecom and water contracts were contacted, what was done to obtain from the managers. According to research tradition, the researcher must find ways of gaining the respondents' co-operation to participate in a research project (Oppenheim, 1998).

The main aim of this section is to show the procedures adopted to collect data from both sides of the transaction to help in the determination as to whether there was contractual balance and good supplier performance. The researcher used a multiple data gathering approach from the buyers and suppliers, the World Bank and government officials. This allowed the researcher to arrive at a conclusion from multiple sources of evidence from different perspectives on PPP contract design and supply performance. In view of this, the key factors that reflected the public sector perspective of pre-contractual power, resource and capability in contract negotiation and the two criteria of supplier performance were considered.

The interview schedule was directed at the managers of Ghana Telecom and Ghana Water Company Limited and senior managers of the service providers. The principal aim was to get first-hand information from the right people. On the supply side, the senior management of both TMP and AVRL and other senior seconded staff were interviewed. Overall, these people were the key decision-makers and implementers, and given their unique role in the whole contract management process, more reliable information was obtained than what possibly could be gathered from lower-level staff that had nothing to do with the transaction.

The research also identified other key stakeholders linked with both contracts. The World Bank was directly involved in the two cases of PPP projects as both the sponsors and financiers leading to the award of the contract. A World Bank representative in the country was interviewed. Second, the interview was extended to include the government side.

The decision to adopt PPP for the utility companies needed political approval, and these informants were major influencers leading to the adoption of PPP for the two projects. For example, the two ministries - the Ministry of Communication and Ministry of Water Resources, Works and Housing Offices - were recognised interested bodies that played a leading role in the contract award and performance of the GT and GWCL respectively.

**Table 5.5 Codes for the Interviewees**

GT and TMP		Water Contract	
PO2	Procurement Manager (GT)	DCEO	Managing Director GWCL
HRM2	Human Resources (GT)	ADO1	Ops/Technical Director (GWCL)
DCEO2	Deputy Chief Executive (GT)	PO1	Procurement Officer (GWCL)
EBM2	EX-Board Member (GT)	AM1	Accounts Manager (GWCL)
AD2	Administrative Manager (GT)	PMU	Project Mgt Unit Director (GWCL)
DA2	Director of Administration (GT)	COP1	Communication Officer (GWCL)
ID2	Internal Auditor (GT)	SM1	Sales and Marketing (GWCL)
PM2	Project Manager	DHR1	Deputy Human Resource (GWCL)
DOO2	Technical Manager (TMP)	DOA1	Director Administration (GWCL)
AD2	Internal Auditor (TMP)	CEOW	CEO Aqua Vitten Rand Limited
OP2	Operations Manager (TMP)	HRM1	Human Resource Manager (AVRL)
COP2	Corporate Affairs (TMP)	COP	Research and Business Planning (AVRL)
		CSM	Customer Services Manager (AVRL)
		WM	Works and Maintenance (AVRL)
World Bank		Government Officials	
Communication Officer: Ghana World Bank Country Office		GOF1 Minister for Private Sector Development GOF2 Minister for Water Resources, Works and Housing	

It was deemed important to capture their perceptions on the PPP contracts. The codes for the interviewees are shown in Table 5.5 and the breakdown of the interviews for each case is presented in Table 5.6.

**Table 5.6 Number of Interviewees**

	Public Sector Interviewees				
Particulars	Public Sector Managers	Govt Officials	World Bank	Service Providers	Total Interviews
Telecom Contract	8	2	1	4	15
Water Contract	9	2	1	5	17

The table shows that 17 interviews were carried out in the water case and 15 for the telecom case. Czaja et al., (1982) recommended that when seeking information from a small group of identifiable people it is necessary to focus on the most knowledgeable people who can provide accurate information.

Furthermore, with the relatively small number of informants, the researcher was able to maintain close associations with the informants and took advantage of being able to ask follow-up questions (Hoepfl, 1997). In gaining access, a telephone call was made to the organisations concerned, the World Bank country representative, and the two government ministers. A follow-up letter was written to confirm the objective of the research and the type of information expected to be collected.

The reliability of the key informants was taken into consideration. According to Miles and Huberman (1994) one of the possible errors of a researcher is to speak to people found to be available, but who might not have good knowledge of the subject matter. To minimise this problem, the researcher made an appointment first with the Managing Director for each of GT and GWCL. These top executives were contacted first as it is the standard practice in Ghana that in order to interview the staff of a public sector controlled body in relation to a research project, permission must be cleared first with the Chief Executive of that company. In the case of the buyers, the MD of GWCL was first contacted and in the case of GT, the Deputy Managing Director was contacted. The pilot phase became useful in confirming that their contribution could be useful to the research. The key informants were selected by their respective companies' CEOs based on the roles each played on behalf of their respective companies in the whole transaction. Three of the recommended managers, two from GT and one from GWCL, declined the offer to participate in the interview. One was then preparing to travel abroad and the other two declined for personal reasons.

## **5.5 Interview Process**

The fieldwork was conducted during a five month period from October 2010 to February 2011. Interviews ranged from one and half to two hours. In all, 28 individuals were interviewed covering both sides of the transaction, (i.e. the public sector and the private sector service providers). However, some of the interviewees were interviewed twice making it to 32 interviews. The Deputy Managing Director for GT and the managers for procurement and Human Resources respectively were interviewed twice in the first case. Similarly, four interviewees from the second case, namely, the Managing Director for GWCL, and the Human Resource and Procurement Officer Managers, were interviewed twice. A follow-up

interview became necessary to address some inaccuracies revealed during the subsequent review of the data collected from interviewees. Although some appointments had to be rescheduled, the interview targets were successfully accomplished.

As indicated by Miles and Huberman (1994) before each interview segment commenced, the purpose and all the key concepts and terminology were carefully defined and explained to the informants. This was done in order to have the assurance that all respondents had a clear idea of the purpose of the research and a common understanding of what the questions are specifically asking for to avoid potential misleading interpretations.

During the pilot study all the prospective interviewees agreed to be recorded, which made it easier to play back the recorded tape in case further checks become necessary. However, at the time of the interview four of the managers asked not to be recorded. To minimise the possibility of missing vital information on what was being said, notes were taken at all the interviews and what was written was read back to the informants for confirmation. Despite the initial view that the level of cooperation from the managers would be low, it actually turned out that co-operation was positive. On reflection, the managers interviewed were very cooperative and the information given was insightful and riching.

### **5.5.1 Documentary sources**

Documentary evidence formed an integral part of evidence for the research. Documentary evidence is a valuable source to improve the quality of the analysis (Yin, 1994). For example, Bryman (2007) noted that documents reveal some important aspects of social reality. An



advantage to the social researcher is that because those documents were not purposely created for the research they represent a reliable source with which to validate the data.

In analysing the issues raised in this study, primary and secondary data were gathered from a variety of sources in Ghana and in the UK. The main sources of documentary evidence are primary and secondary data. These are made up of published and unpublished documents, company reports, committee reports, and newspaper articles. Both GT and GWCL, together with their respective suppliers, had their corporate websites analysed for relevant information leading up to, and subsequent to, the signing of the contract. In the GT contract, evidential value was obtained from a ministerial report that investigated the operations of GT from 2001 to the eventual sale of GT to the private sector in 2008, and part of the report covered TMP's management tenure. GWCL's published reports from 2006 to 2010 were analysed, including various press reports. The list of documents is depicted in Table 5.7

**Table 5.7 List of Documents Analysed**

Item	Particulars
1	GT Memoranda./Files
2	GWCL Memoranda./Files
3	Newspapers, Articles Local and Foreign, Staff newsletters
4	Policy Document on PPP Private Sector Development
5	Inter-ministerial Report on the sale of GT to Vodaphone UK
6	GT Audit Reports 2002-2005
7	GWCL Audit Reports 2005-2009

In addition, information was obtained from newspaper and magazine articles. Lastly, other sources of evidence were obtained from World Bank reports and newspaper articles. These

documents though limited in their uses have proved useful in providing valuable information and insights about the two PPP projects (ie policy issues, management and outcomes. However, documentary evidence has obvious limitations. Official documentation may not contain all information and could also be biased (Scot, 1990). For these reasons, they need to be used with caution. However, as Yin, (1989) has stated ‘Because their overall value, documents play an explicit role in any data collection in doing case studies.’

### **5.5.2. Data Processing**

The aim of this section is to discuss the data processing method for the analysis and interpretation of the data in the research. A large volume of data was produced and had to be taken through various stages of processing. Since the interview questions are qualitative in nature, there was a need to identify and evaluate their relevance to the main study.

Eisenhardt’s (1989) two-stage method of within-case and across-case analysis guided the analysis of the interviews. The method involved writing up a summary of each individual case in order to identify important case level phenomena. Following this process, a coding scheme was developed to assist with the cross–case analysis with a view to sorting out the patterns to obtain an overall view of the cases being studied. Coding is a way of sorting information from a mass of data into distinctive categories and labelling them according to their characteristics (Miles and Huberman, 1994). The coding scheme was specifically helpful at the analysis stage to capture the pre-contractual power variables operationalised (i.e. utilities, scarcity and information), the variables for resources and negotiation capabilities (see Appendix B)

Using the coding technique what was considered was the independent and dependent variables, categories, and patterns (Miles and Huberman, 1984, 1989). Coding alpha numerals is assigned to each of the power variable of utility, scarcity information, in the first independent variables. Each is further categorised using the topic guide and the research questions. For example the pre-contractual power relation was further coded into operational and commercial, scarcity and information. Each theme was further categorised using the topic guide and the research questions. For example the pre-contractual power relation was further coded into operational and commercial, scarcity and information. In relation to dependent variable of post-contractual balance /imbalance is further categorised into the risk sharing in fixed assets and incentives design. In the second stage, the initial groupings was later refined and reviewed and then filtered them through several stages to arrive at a clear pattern. Attempts were made to use the Nvivo package, but this was abandoned in favour of a manual technique because the software was not helpful in mapping the various variables as intended. When the above steps were taken, it was possible for the researcher to give an answer to the research question and to form a conclusion about the whole case study.

### **5.5.3 Alternative Methods Considered**

In the research tradition, there are many research approaches to gather data and also different ways to measure a phenomenon. The question of whether to use alternative approaches is determined by the purpose to which such an approach can add to the value of the research. In some cases, alternative methods may be appropriate to offer alternative views. In this sense, a combination of different types of data would have been desired.

In relation to measuring the variables in the research, alternative measure such as Likert scale were considered to ensure that findings are supported by other measures. This could have created a need to engage in the complicated process of weighing opinions by rating such criteria, and there is no doubt that some researchers would have felt compelled and excited to do so by using statistical analysis tools. This was not the case here, and the justification was provided by the fact that the interviewees in both cases exhibited sound knowledge and judgements in analysing the problems confronting them in the management of the contracts and had good idea what went wrong. Their views and perceptions were candid and they were able to provide their own assessments on the key variables and their bargaining positions with the suppliers thus rendering unnecessary further weighing and ranking their view to give meaning to what their perceptions.

The use of telephone interviews and questionnaires was considered. However, given the sensitive nature of the issues involved in the two cases, the use of telephone interviews was eliminated, as it was considered security risk and participants prefer direct face to face interviews. This could be explained by the point that respondents might be hesitant to disclose confidential information in such a way and that could undermine the integrity of the answers and their value for the research.

In the case of using structured questionnaires, this was considered but dismissed as it was felt that it would limit further probing and discussion on the number of issues that came up during the interviews. Using the quantitative approach as a form of triangulation, as already explained, may lead to duplication and using that approach on its own might not be helpful in exploring deeper the constraints that public sector authorities face in developing post-contractual balance. Considering the number and duration of the interviews and considering

that five different actors (two each from the public sector and the private sectors and the World Bank) and government representatives and the variables and indicators used, providing an alternative method would not offer the necessary advantages expected. In practical terms such a task would be difficult to complete because of the sheer volume of work involved and the repetitive information obtained from the original discussion. On the other hand, the volume of information will not only be confusing but will be difficult for the readers to read and understand the key points that the research seeks to highlight. In the end, it may not add any new evidential value to the research to justify additional resources used in the exercise. More importantly, a good research practice requires that a good researcher should access his or her work and know when to stop collecting further data (Morgan, Eisenhardt, 1989; 1998).

#### **5.5.3.1 Objectivity and Validity**

Maintaining research objectivity in qualitative research is of paramount importance to researchers (Miles and Huberman, 1984; 1994). For example, the tools used should be able to measure the data that reflects and describes the true state of power relations in the project by mapping the outcomes against set standards. In addition, maintaining objectivity and minimisation of research bias provides the assurance that the findings and conclusions can stand strict scrutiny. In order to meet research standards that satisfy the reliability of findings, the research process has been made more rigorous in many ways. First, the questions were designed guided by the hypothesis and the epistemological position of positivism underpinning the research. This is clearly outlined so that readers are informed of what knowledge is to be arrived at. Additionally, the research is triangulated at different levels so results are, as far as possible, mutually self-enforcing and self-checking.

The following protocols were observed, following Bourque and Fielder (1995). The draft questions were pre-tested in the pilot study using the administrative procedures that would be used in the study. Furthermore, as part of the preparation towards data collection, all conceptual issues were clarified with the informants and areas prone to bias were identified beforehand and addressed. A standard interviewing format was adopted and followed consistently throughout the data collection exercise. Additionally, a strict regime of field and observation note taking was followed alongside the interview recordings. The objective was to compare what was captured in the electronic recording as a way to validate what information was recorded.

Furthermore, care was taken to minimise bias during the selection of what evidence is relevant and what is not. Thus all informants were given equal opportunities and encouraged to comment on the same issues as previous respondents. This was one of the effective methods used to ensure that the research subjects and topics were kept central to the research. This is to avoid misunderstanding of the meaning of what was said as well as to help put each theme in its proper context before the data was analysed. The feedback loop also provided a solid basis for checking consistency and contradictions at the analysis stage. An objective picture was also built by interviewing both the suppliers and the public sector for their perspectives. The information obtained was later discussed with respondents for their feedback. Both perspectives were consequently used for intra-triangulation and inter-triangulation to further enhance the objectivity of the research findings.

As is the case in semi-structured interviews of evidence gathering, reporting depends on such factors as the subjective state and the personal and cultural frames of the researcher. These may involve influencing persons to describe what constitutes factual issues and what

constitutes inaccurate information on such topics. However, neutrality is upheld at all times by avoiding the problems of interviewing, by minimising giving off body language to suggest responding in a particular way.

Finally, there is also a sound caution in social research that a researcher must take care not to be biased in selecting what appeals to the researcher and ignoring important ideas. This is of particular importance in qualitative research where the researcher is deeply involved as a participant in gathering information, selection of method of analysis and interpretation of research outcomes, where the criteria that apply in judging validity differ from those of quantitative methods. With this in mind, and observing best academic research practice, the combination of methods employed in this study took into consideration all these problems to engage in a fair and objective presentation of the information.

## **5.6 Conclusion**

This chapter has described the research strategy used to test the hypotheses of the three risk factor model developed in Chapter 4. The chapter has discussed the major research paradigms and research strategies mostly found in management research in forming the research objectives and qualitative case study was employed in the structuring the primary research requirement. An important part of this chapter was devoted to the description in detail of the definitions and operationalisation, and of the constructs and indices used to measure them. In the next three chapters we examine empirically the two cases.

## **CHAPTER 6**

### **The Ghana PPP Contracts: GT and GWCL**

#### **6.1 Introduction**

The previous chapter laid out the methodological framework for the gathering of evidence. In Chapter 1 we noted that private-sector participation enables governments to develop infrastructure and service provision at a cheaper cost than under traditional procurement practices. The large and growing literature on PPP policy in Western countries have emphasised the importance of private sector involvement in public sector infrastructure and service provision. In this chapter we discuss the two PPP cases and analyse two different public provisions within the public sector one in the telecoms sector and the other in the water sector. Each case provides description of management contracting of PPP and the structure of power, post-contractual balance and supplier performance for the specific public services analysed. Particular attention is paid to conditions that led to the public sector reforms in each case and the political and financial context within which PPP policy is implemented in Ghana. This will allow us to understand the internal and external environmental factors affecting the participation of the private partners and the expectation of the efficient outcomes. The chapter is structured as follows. Section 6.1 discusses the factors that led to the introduction of private sector initiative. Section 6.2 discusses the political context of the PPP reforms. Section 6.3 examines the GT's operational and financial problems and the introduction of a private sector partner to manage the company. In the second case, section 6.4 highlights the background problems of GWCL. Section 6.5 examines the problems in the water company and the award of the water contract to a private sector company.



## **6.2 The Ghana and PPP policy**

In countries like UK and USA the combination of public and private sector commitments contributed to impressive results in areas of health, education, roads and IT projects which are key areas to national development. There have also been criticisms against the use of private sector in public provision as costly. However, its relevance to World Bank economic policies in developing countries is best illustrated in the centrality of private sector participation in its strategic policies (World Bank, 1989, 2002). The Business Partnership an outreach group of the World Bank, developed broad policies with International Finance Corporation (IFC) and Multilateral Investment Guarantee Agency (MIGA) all affiliates of the World Bank to work with other international and governmental agencies to increase the awareness and adoption of private sector model into their developing agenda in low income countries (World Bank, 2002, 2004). In Ghana, the driving force may be identified as economic, political and social interventions to support failing public sector services.

### **6.2.1 Factors Driving PPP Reforms**

Before and after independence in 1957, all public utilities were under the control of the state. The state continued to manage public utilities providing subsidies well until the 1980s when the economy began to flutter in the wake of world financial crises. By 1990 through to 2000, Ghana's debt has increased beyond safety levels and micro economic indicators such as annual growth rate reduced from 12.2% in 1983 to 9% by early 1990's and inflation has increased with standard of living falling drastically (World Bank, 1989, 2002). This brought along other problems.

The government could no longer support the utility companies with the amount of subsidies required to keep services going. In addition, condition of the infrastructure of these utilities was fast deteriorating and internal generated funds were not sufficient to support normal operations. Furthermore, mismanagement, and excessive bureaucracy affected the financial performance of these public companies. This in turn, affected their ability to raise sufficient funds to run and expand services to meet demand. It is within these challenges that the two state-owned utility companies; telecoms and water services came to sharp focus as the most affected utility companies in the country. Frempong, (2007) reports indicate that limited resources of GT created a big gap in customer demands for improved and expanded services. In the case of the piped water supply, water coverage was low although government's financial support has been sustained over the years to keep supply of water to the people. Although general access to safe water supply appears to have improved, increased population drift to the urban centres and demand for more water indicates that there was a need to pursue aggressive policies to modernise infrastructure and improve services.

The other reason for the reforms has to do with the weak capacity of governments and its rigid bureaucratic administrative structures that also contributed to poor quality of public services, high transaction costs, and widespread corruption resulting in inefficient management (see World Bank, 1989; 1996; Larbi, 2008). The World Bank, on its part recognised that given the state control and poor public management of telecommunication and water sectors, opening it for competition would address these problems effectively.

### **6.2.2 Political Context of PPP reforms**

The first significant step towards privatisation in Ghana was the implementation of the World Bank's Accelerated Development Plan (ADP) in 1994. The initiative was one of several long-term policy frameworks aimed at transforming the publicly controlled utility companies through a gradual transition towards privatisation. For example, it sets the agenda for introducing private operators and competition into the industry and for its eventual privatisation (Haggarty et al., 2002; Ahoritor, 2003; Frempong, 2007). The recommendations under the ADP framework for public utilities are a sale or a form of partnership or similar private sector participation schemes. The decision to privatise or not in many ways generated a lot of debate and controversy in the country between the World Bank and the government, civil society and interest groups.

Despite the urgent need for public procurement reforms, the orientation for the political leadership was not entirely pro-market even though the rule of law remains strong in the country (Larbi, 1998). This partly accounts for the delay in the implementation of PPP reforms in the country. There is evidence that the idea of privatisation was welcomed at the time, however, the government was reluctant to sell public utilities to the private sector for political reasons (Haggarty et al., 2002; Whitfield, 2007; Frempong, 2007).

Another problem was that potential private partners were reluctant to invest in developing countries perceived to have weak legal structures to protect their business interests (Caves, 1996; Tan and Litschert, 1994). Given the political context in Ghana and its nascent liberal democracy, the international service providers wanted assurances that their assets and

interests will be protected against state expropriation. Thus strong political commitment from the government had to be provided to assure the international suppliers about the safety of their investments. In addition to the need for property rights protection, appropriate institutional structures to facilitate sound project implementation are required to be put in place by the government.

### **6.3 The 1980s: A Decade of Decay and Delays**

#### **6.3.1 Ghana Telecom**

In Ghana, GP&T could not respond to the growing demand for more telephone services and improved quality coverage. Analysis showed that the distribution of telephone services across the country at this time was low. Even in the 1990s only 3 out of 1000 inhabitants had access to a phone, and even this low level was limited to urban dwellers (Frimong, 2007). Accra, the capital, accounted for about 57% of the total lines in the country, yet in this period, demand for telephone lines increased dramatically. Experts estimated that demand at the period was over new 150,000 lines per year, while supply increased by only 1,000 lines a year.

Subsequent feasibility studies conducted in the 1990s showed that the realistic projected demand was between 300,000 and 500,000 lines by the end of 2020 to meet growing local demands and international standards (Ghana Vision 2020, 1997), and by 2002, statistics showed that Ghana had in total only 455,000 telephone subscribers both fixed and mobile subscribers (see Table 6.1).

**Table 6.1 Basic Telecommunications Network Indicators**

Particulars	Level of Access
Total no. of telephone subscribers fixed-mobile)	455,000
Total fixed line subscribers	225,000
Mobile system subscribers	230,000
Total number of subscribers (per, 100 inhabitants)	2.08
Waiting list for main lines	15,567
Mobile subscribers per 100 inhabitants	0.93
Main Telephone line (Residential %)	42.0%
ICT	
PC (per 1000 persons)	3
Internet Hosts	235
Internet Users (per 1000 persons)	40500

Source: ITTU World Telecom Indicators (2002) and National Communication Authority

Internet user growth was also hampered due to the inadequate infrastructure of GP&T. Surveys showed that internet services were low in the country and limited to a few large businesses in the financial institutions, government and corporate bodies (Osiakwan, 2003; Dzidonu, 2004). In the educational sector, the picture was not encouraging either. About 79% of secondary schools were reported to have an average of 19 computers to support both administrative work and teaching (Dzidonu, 2004). Thus emphasis was placed on increasing broadband services and extending them to other educational institutions not yet connected at all.

Under the ADP plan in 1994, the telecommunication sector was proposed to be re-structured as follows:

1. The sale of GP&T to local or foreign investors
2. Partnership deals on Build Operate and Transfer or similar private sector participation schemes
3. The establishment of a regulatory body.

A significant step taken in the reform process was the separation of the postal services from the telecommunications, which led to the creation of Ghana Telecom (GT). The separation was strategic, in that it was meant to make GT attractive to prospective investors. In addition, an independent regulatory body, the National Communication Authority (NCA), was established in the same year to regulate the activities of various private operators, including the formulation of policies and quality standards.

Despite many positive efforts to transform GT into a modern telecoms company, its technical and operational problems remained unsolved. It is important to note that the problems of GT were not confined to only financial, but also has managerial challenges. Many attempts were made in the past to inject capital into GT to improve infrastructure development but the supervision of the projects was not properly handled by the GT management. For example, as part of the telecommunication rehabilitation programme, a project known as the Second Telecommunication Project (STP) was initiated in 1988.

**Table 6.2 Source of Funding for STP in Million USD**

Source	Foreign	Local	Total
Government of Ghana	1.5	9.8	11.3
France (CCCE)	21.7	-	21.7
Netherlands (NKF)	18.8	-	18.8
Japanese Grant (JICA)	9.2	-	9.2
Japan (EXIM)	7.0	-	7.0
Japan (OECF)	69.5	6.7	76.2
Ireland	1.7	-	1.7
IDA	18.3	0.7	19.0
Ghana P&T	2.3	5.5	7.8
Total	150.0	22.7	172.7

Source: P&T Corporation, 1993 (in "The World Dialogue on Regulation for Network Economies (WDR).

The government, through the World Bank and other multilateral donors in 1988, made available US\$173 million to provide further rehabilitation; upgrading and expansion of the telecommunications facilities in the country (see Table 6.2). This was to be completed by 1991. Unfortunately, as a result of managerial incompetency and political interference, the project was completed three years behind schedule (Haggarty et al., 2002). As can be seen from Table 6.2, the vast majority of funds for STP were foreign – US\$150 million out of US\$172.7 million.

However, despite all of the inadequacies of GT, when the decision was taken to privatise it, local opposition delayed early implementation. The government on its part however, realised it had no choice in the matter if it was to solve GT's increasing financial and operational problems. As a compromise, and in 1997, the government brought in Telecom Malaysia (TM). Under the arrangement, TM bought 30% of GT shares for US\$38m, but with 5:3 majorities on the Board and promises of further investment funds (Haggarty et al., 2002; Frimpong, 2007; Amin, 2007).

However, the Malaysian company reneged on those promises and, in 2002 the new NPP government led by Mr. Kuffour decided to change the composition of the Board from 5:3 to 3:5 to reflect on their shareholdings ratios. TM rejected these changes and subsequently sold back its stake in GT to the government for US\$55m. Consequently, GT control reverted back to the government, but now with even more financial problems: The government had to find money both to settle TM compensation and to provide further capital to keep the GT operations going. To make it worse for GT, the International Financial Corporation (IFC), a

member of the World Bank withdrew an earlier approved loan of US\$100 million from GT as a punishment for disrupting the privatisation process (see Haggarty et al., 2002).

### **6.3.2 The GT Contract with Telenor PPP**

Shortly after the TM debacle, in the same year 2002, the government finally took a decisive step to experiment with private participation idea under the banner of public-private partnership based on the policy guidelines of the World Bank. The new government was convinced that the poor operational and commercial operations of the GT could be reversed to make it more viable to meet domestic and business expectation including prospective foreign investor's is reliant on the private sector initiative (Frimpong, 2007).

Following a tender process that resulted in one bidder responding, the contract was awarded to Telenor Management Partners (TMP management consulting partners from Telenor Norway in August 2002. The management contract was signed in January 2003 for a three year mandate under which TMP is to take over the operations and management of the company. It was subsequently extended for an additional year. As part of the terms the private partner is to take over the management of the company under a three year contract.

The specific targets for Telenor in the 2003 agreement are summarised as follows:

1. Telenor to provide a minimum of 400,000 fixed lines and 750,000 mobile phones by 2005.



2. Install and fix broadband to every telephone subscriber in every town, including secondary schools.
3. Provide Ghana Telecom with management expertise and technical services.
4. Improve the quality of service on the existing infrastructure and introduce multi-media applications including the internet and e-commerce
5. Develop and implement a human resource strategy for GT.
6. Develop effective methods to investigate malpractices in the telecommunication sector

Under the terms of the contract, the Ghana government was assigned the responsibility of providing investments funds for the infrastructure and equipment required for the project. The government signed a loan agreement with the World Bank and also got some financial support from other multilateral donors to implement the telecoms projects.

The government expected the project to provide social and economic benefits and revenues from operations. Firstly, savings is expected to come from a number of areas. It is assumed that the incoming private sector partner would put in place measures to reduce losses from fraud and staff malfeasance and waste. Secondly, it is projected that political interference that had resulted in poor management of the company's affairs will be minimised leading to high staff productivity. Thirdly, the private sector model is expected to undertake revenue generating activities through its expansion programmes and also generate savings through the introduction of business-like models and commercial work practices.

## **6.4 Ghana Urban Water Contract Case**

### **6.4.1 Background to the Case**

The Ghana Water Company Limited (GWCL), formerly called the Ghana Water and Sewerage Corporation (GWSC), was established in 1965 as a state-owned company responsible for producing and distributing water to the people of Ghana. It also had the responsibility of managing the sewerage system in the country. GWSC operated as an integrated state utility company until 1999, when the sewerage and rural water segments were separated from the core water supply operations. Following this, GWSC was changed to a liability company and was solely responsible for the management of Ghana's urban water supply under a World Bank Urban Water Project.

Similar to GT, the rural water segment from urban water was to make the urban water project more attractive to prospective investors. The rural water segment came under the control of the Community Water and Sanitation Agency (CWSA) with the responsibility of managing water supply to the rural areas; discussions of this company are outside the scope of this study.

Prior to 2005, the idea to privatise urban water in Ghana was first proposed by the World Bank as far back as 1994 (Katharina, 2001; Finger and Allouche, 2002; Lobina and Hall, 2003). This was also in line with the official UN recognition in 1992 that “water has an economic value in all its competing uses and should be recognised as an economic good” (Quoted in Castro, 2007, p.27).

GWSC's financial position was made worse by the fact that the company could not raise sufficient revenue from its operations to run the company independent of government financial support. One key reason for this was that the company was losing revenues through water losses from water leakages, bursting of old pipes and illegal connections. At the time water losses through inefficiency were as high as 50%, indicating that the company was getting only half of its potential income. The other reason is managerial problem. Lack of motivation, politic interference and bureaucracy affected water operations. Lack of adequate funding played a key role in the deplorable condition in GWSC infrastructure.

Statistics available showed that people with access to potable water were not encouraging despite financial support from international donors. The percentage of people with access to water dropped from 76% in 1992 to 59% in 2002. Accra, the capital city, has a 3million population but just about 60% of the people had access to good drinking water (Whitfield, 2007). As a result, water was rationed to certain parts of the city on either a daily or weekly basis, while some rich households had to rely on expensive water tankers services for their daily water needs. The situation was even worse in other urban areas in the country, where some communities went without water during dry spells that last more than three months.

The cost of infrastructure and rehabilitation of water systems and expansion works was estimated at \$1.8billion (Foster and Pushak, 2011; Whitfield, 2007). As a first step towards privatisation, however, the Ministry of Works and Housing commissioned a series of consultancy groups, Halcrow from the UK and Louise Berger from the US, to study and made recommendations on GWSC's operations (Katharina, 2001; Whitfield, 2007). The Halcrow report concluded that GWSC's poor performance was the result of inadequate

financing and managerial inefficiency. Based on its findings, the report recommended handing over the urban water services to the private sector to manage. These recommendations had political backing from the IMF and the World Bank, who used this recommendation and intensified their pressure on the government to bring in private investors to manage the urban water segment.

#### **6.4.2 Move to the Market**

Private sector involvement in the provision and distribution of potable water to the urban areas was given further impetus when the government could not raise about \$1.8 billion for both expansion works and rehabilitation works to meet MDGs target of getting water to all communities by 2020. The government had nowhere to turn other than the World Bank. That meant the government had to consider the question of privatising water services for which the World Bank had been pushing all along.

However, two critical issues delayed early water reforms. First is lack of political will on the part of the government given the intense civil society opposition to any form of privatisation of the water sector. As is always the case in developing countries, the argument against water privatisation was centred on the need to protect public interest against commercial exploitation by the private sector. Sustained opposition by trade unions and civil societies on one hand, and the government's own reservations concerning the political wisdom of privatising water on the other, were the internal issues that delayed early implementation of the reforms (ISODEC, 2001). The other factor was external. Due to political risk concerns, the government was finding it hard to find a foreign investor to invest in the water sector

anyway. Meanwhile, GWCL operations continued to worsen and many people were denied access to water.

### **6.4.3 The AVRL PPP**

The World Bank came to the conclusion that only hard conditions through project financing policies could force the government to undertake procurement reforms (Martey, 1991). Eventually, the opportunity to restructure the public utility sector came when the government under Kuffour came to power in 2001 and decided to apply for World Bank debt relief under the Heavily Indebted Poor Countries (HIPC) programme. A HIPC programme is a World Bank debt relieving policy in which countries whose debt portfolio has become unsustainable, and therefore difficult to service are offered a way out for all of its debts and by which all outstanding debts are written off under strict conditions and supervision (Whitfield, 2007; Frimpong, 2007). When Ghana opted for HIPC, the World Bank made water privatisation a key condition for writing off the country's debt and providing further financial support for the rehabilitation and extension of urban water coverage in the country (Whitfield, 2007, Frimpong, 2007). This was a turning point in the history of the GWCL. Even so, it took the government another 4 years before a suitable partner was found, largely because investors felt that the country's political and economic environment was not secured for private investment of such magnitude.

After the government succumbed to World Bank pressure, the choice of a PPP framework created a stalemate. Ghana favoured the Build Operate and Transfer (BOT) scheme but the investor community showed no interest, as they regarded it as too risky. However, the few

foreign investors who indicated their interest in the two projects rejected any PPP arrangement that would require them to invest in the water company. As a result, the proposed lease contract was rejected. Eventually when it became clear that no foreign company was willing to enter into a lease contract with government on GWCL project and that there was no suitably qualified local private company in the country, the World Bank confronted the government of Ghana with two options. If the government pursued a management contract with the private sector, the Bank would provide \$100million and leverage other resources for an additional \$30million. On the other hand, if the management contract option was rejected, then the Bank would provide only \$30million (Whitfield, 2005; World Bank, 2004a). Convinced that there was no other choice, the government chose the World Bank's option with tacit approval of the interested international suppliers.

In the tendering process, three companies of Saur of Paris, BiWater of the UK and AVRL, from Netherlands. Out of the three AVRL submitted its bid documents as Saur, and BiWater withdrew their bids. The contract was consequently awarded to International BV of Netherlands of Netherlands; Ghana government signed a 5 year contract with Aqua Vittens Rand Limited (AVRL) in 2006). The management company AVRL is formed by two consortia Vittens International BV of Netherlands and Rand Water Services of South Africa. The specific targets for AVRL in the 2006 agreement are summarized below.

1. Reduce non-revenue water losses from the current levels of 48% to 26% by 2011
2. Install 50,000 new household connections and 350 public stand pipes in designated areas

3. Assist the GWCL to improve the management of the water sector and pursue its long-term financial viability strategies
4. Reduce customer response times
5. Reduce chemical usage and content in water
6. Reduction of staff per 1000 connections to below 10.

The contract covers 80 urban water systems and is financed from a World Bank grant of \$103million, with Nordic Development support of \$5million and \$12million from the Ghanaian government itself (World Bank, 2004a, 2004b; GWCL, 2010). Under the contract GWCL management is responsible for providing fixed asset and for monitoring the AVRL executives with the assistance of a financial technical auditor. Thus the introduction of private sector initiative seems to hold high expectation both from the government, the World Bank perspective that genuine partnership has been put in place that would lead to significant improvement in GWCL operations and finances (Whitfield, 2007; Katharina, 2001).

Several areas were identified for basis of savings. The government and the World Bank expected that the incoming private sector partner will apply market-led principles in the management of the company to make savings. AVRL executives were expected to introduce standardise its procurement portfolio and reduce the incidence of non-revenue water losses to improve financial performance. In brief, the Ghana Urban Water project is an international collaboration arrangement involving the Ghana government as the main client, AVRL the service provider, the World Bank and other donors as the financiers for the water project.

## **6.5 The Structure of the Telecoms and Water Management Contracting of PPP**

The management of the two PPP projects in developing countries is complex. They are made of three major stakeholders of Ghana government, the contracting country, the private sector partners and the World Bank and other multilateral donors as project financiers.

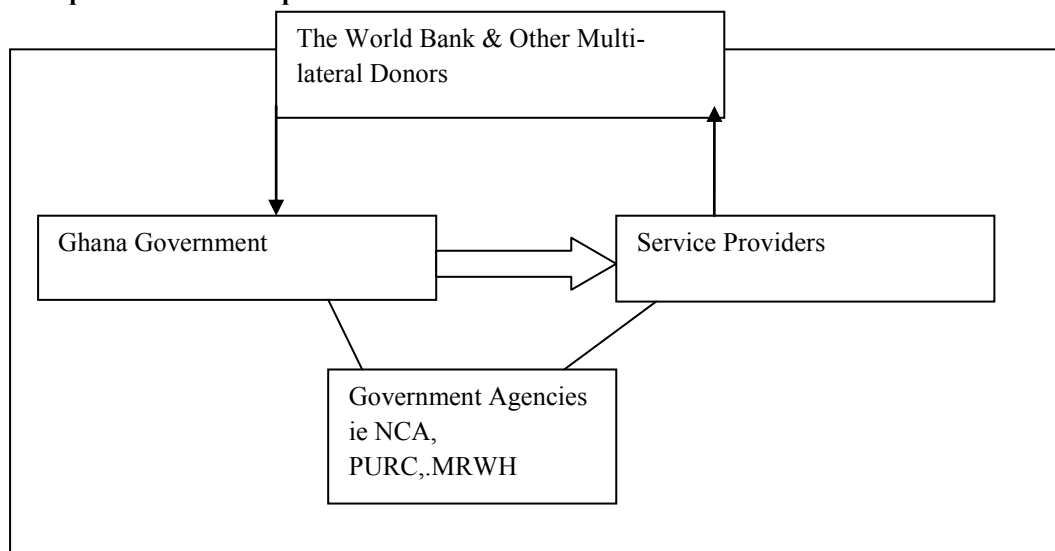
Under this typical management contracting, Ghana government is the principal party contracting on behalf of GT and GWCL. The government is responsible for the provision of the required capital for the two projects tendering, selection and award of the contracts. Internally, there are many individuals and government ministries who also perform some specialised functions. In a typical public sector administrative structures in Ghana, sector ministries exercise oversight responsibilities over agencies and organisations under them. This means GT comes under the Ministry of Communication while GWCL is under Ministry of Water Resources, Works and Housing (MRWH). Regulatory bodies were put in place to deal with specific issues of exploitation, quality and standard of performance; namely Regulatory Commission (PURC) for water and National Communication Authority (NCA) for telecom operators in the country. A Project Management Unit (PMU) is set up by the government to for that purpose for planning and implementation of the two projects to meet planning objectives.

The next stake holders are the private sector partners working in collaboration with the government in the telecoms and water contract. A private sector partner is expected to execute the contract according to government requirements and specifications which in this case identified as TMP and AVRL respectively.



The last major stakeholder is the World Bank. The World Bank is responsible for providing loans to the Ghana government to finance the two projects. Although these stakeholder have a different role to play in the implementation and execution of PPP policy in both the telecoms and water contract the structure is like any typical network with their activities interlinked. In recent years, the role of the World Bank has taken a centre stage in PPP policy implementation in developing countries and seeks to control the direction of the project through its project technical and financial support.

**Figure 6.1 Tripartite Relationships in the Telecoms and Water Contracts**



On one hand, the World Bank would want to minimise financing risks in the projects and does so through conditions attached to the loans. Typically, the condition includes competitive tendering, project implementation milestones and reporting and withholding of funds for missing specified key indicators. The structure in Figure 6.1 indicates that the government depends on the World Bank for financial support on one hand, and on the private

sector on the other to meet its stated objectives in the two projects. The private sector on the other hand, revenues is dependent on the Ghana. This is the general structure of collaboration that shapes the implementation of PPP in Ghana.

## **6.6 Conclusion**

This chapter has presented the background of the study which is the subject of the empirical study. There are three major stakeholders, the government, the service providers and the World Bank. There are two issues of interest here. While the objective of private sector companies is to maximise profits from the relation, Ghana government on the other hand, has set of objectives to maximise welfare benefits in the form of increased functionality at reducing cost. Both the government and the private sector can achieve their objectives when risk and uncertainty are appropriately allocated between them. Given the economic rationale for PPP initiative regarding mutual risk sharing it is worthwhile to empirically examine both the telecom contract and the water contracts whether the empirical evidence supporting this assertion is strong. In the next three chapters, the empirical study examines the relationship power between the government both in the GT and GWCL with the TMP and GWCL respectively.

## **Chapter 7**

### **Presentation of Interview Data**

#### **7.1.1 Pre-contractual power resources of GT and TMP**

This section presented the interview data obtained from GT-TMP telecoms contract using semi-structured interviews. From the data obtained from the research the contract management strategies of all the parties are analysed and the impediments and facilitators to post-contractual balance are highlighted. Particular attention is paid to conditions that enable the public sector to obtain key power resources both structural and external which post-contractual balance is dependent to facilitate good supplier performance.

The discussion of the results of the interview is presented in two parts. The first part relates to the key characteristics independent variables of pre-contractual power influencing the design of a balanced contract while the second part relates asymmetry in resources and negotiation capabilities and other factors that may be found to have positive impact on the development of post-contractual balance. General perception of all interviewees, as well as differences in perception between the public and private sectors parties are presented. After this presentation of data, the author provides analysis within the context of determining power relations. The chapter is structured as follows. Section 7.1 presents the interview data on two independent variables of pre-contractual power resources and resources and negotiation capabilities from the GT side. Section 7.2 presents the supplier side of the interview. Both the interview results are analysed and evaluated their pre-contractual power structure in section 7.3. In the second part, the interview data on GWCL and AVRL and the results are analysed.

### **7.1.2 Independent Variables Utility –GT interview Data**

The main interview was preceded by asking interviewees from the public sector managers and the private sector representatives in order to confirm the evidence obtained during the pilot stage that PPP telecom contract contained significant asset specific investments and switching cost. At the pilot stage, it was established that the PPP contract asset specificity and switching costs were involved. After obtaining the confirmation, further discussion on its effect on the contract relation was deferred until later part of the post-contractual balance analysis stage. The consequently interview shifted to the next stage which is obtaining evidence on pre-contractual power resources from the interviewees.

Operational Importance: Interviewees were asked about relevance of the telecoms contract with the private sector. First, there was broad agreement that the partnership was established in order to address inadequate telecommunications infrastructure, and service delivery problems in the country. At the heart of GT's problems was financing requirements to rehabilitate and modernise the telecoms equipment. The Deputy Chief Executive (DCEO) explained:

‘Our telecommunication services were down at the time and, we could hardly serve our customer’s needs for fast and reliable telecom services. All the existing equipment in use were old and could not handle a large volume of traffic, particularly international calls, at one time’.

The GOFI also added that the past government decided to take immediate action to sort out the basic infrastructure financing needs of the company to keep operations going but unable to meet these financing needs from their resources. It emerged from the interviews that other options were explored including privatising the company’s operations but the deteriorated

nature of the existing facilities was unattractive for buyers. The other reason given was that the Ghanaian public opinion was against the privatisation. The government minister (GOF1) revealed that as a result of public agitation against privatisation the only option was to seek external funding and that took them to the idea of forming a partnership. He admitted that:

‘Without the partnership with TMP, GT could face serious operational problems of inability to meet customers demand for telephonic and internet services. The investors we are encouraging to invest in various sections of the economy required efficient telecom services and that responsibilities falls on our telecom company.’

Other interviewees (DCEO, AD2, and PO2), although not entirely happy about private sector involvement in the company’s management, agreed that TMP’s partnership allowed GT to expand its services, enabling the government to keep vital telecoms services operational by serving the business and domestic needs of the people including extending internet facilities to schools in the country.

Strategic Importance: On the issue of the strategic importance of the telecoms contract the Minister for Communication (GOF1) described the telecommunications contract as follows:

‘We considered the sector very important as the key area to provide infrastructure base to support foreign investors... our economic development and our ability to attract investors into the country depended on GT being able to provide a reliable, good telecommunication network in the country... At the time we signed the telecom contract GT operations had almost ground to a halt... barely covering five per cent of the service area in the country.’

The government minister (GOF1) confirmed this problem and added that the rehabilitation and survival of the telecommunications infrastructure was important to the achievement of Millennium Development Goals, and maintenance of national security.

On the importance of TMP services to GT's vision run a modern fast and cost effective telecommunication services, the view of the interviewees was that they considered the service provider as key to the ability of the government to attract investment and ICT development into the country. The DCEO noted:

‘Our country can only develop its economy when we have effective communication networks, and increase ICT knowledge in our educational institutions for rapid technological development. We could not have achieved these objectives using the old systems and equipment we had at the time. ‘These were our priorities we sought to achieve with the help of TMP.’

There were other compelling reasons for the TMP contract which is to with government policy to improve with computer literacy in schools and computerisation of government business for national development and economic growth.

As GOFI and DCEO both explained the survival of the telecom industry is important to the government and pointed that its poor infrastructure meant that they were losing their market share to private mobile telephone companies. He explained that:

‘Our rivals “Areeba” and “Mobitel” have virtually taken our market because our customers were becoming dissatisfied with our services and were changing from fixed lines to mobile phones services offered by our rivals. Analysis done by our experts and the World Bank recommended that we bring in private sector partner to manage the facility for us and the Bank will provide funding.’

According to the DCEO and GOF1, the government was reluctant to engage a private sector partner but had no option than to form the partnership that brought in TMP.

### **7.1.3 Scarcity: Available of Suppliers**

This section presents the interview responses to questions about the availability of number of suppliers for competitive bidding for the telecoms project.

Although the interviewees acknowledged the importance of competitive bidding, they believed that this objective of getting value for money was not achieved in this particular contract and was attributed to lack of competitive bidding leading to the award of the contract to TMP. The reason given for lack of many suppliers was two-fold. The first is related to limited suppliers in the telecoms market. Two interviewees DCEO and COP2 explained that the global telecommunications market is technological based and complex and restricted to only specialised suppliers. GOF1 observed:

‘Our search on the international market revealed that few suppliers were active in professional management services in the telecom industry and the response from those qualified operators were disappointing’

The other reason given is to do with the unwillingness of foreign suppliers to work with the government. According to OP2 going to the international market has its own challenges which he attributed to investors fear of investing in the country. As he explained:

‘Potential foreign partners we got to know feared to invest in the country because of our previous track record of nationalising foreign companies during military rule in the 1980s.’

According to the government official, only TMP remained interested in the contract up to the preferred supplier stage even though the vacancy was widely advertised. He further explained that:

‘We got the three companies who indicated their interest in the project and upon inspection and found the poor state of our infrastructure and systems withdrew their interest.’

To complicate matters for GT, they found out that no local company was qualified to compete and win the contract in terms of resources and experience. It was evident from the interviews that attracting qualified and willing foreign suppliers to bid for the telecoms contract became difficult for GT. DCEO expressed disappointment that they could not attract potential suppliers for the project.

Beyond the problem of supplier scarcity there appears to poor handling of the selection process. The question as to whether TMP selection process was transparent interview responses were varied and mixed but the general impression was that it was not transparent.

A former GT manager (OP2) who observed that the selection process as not transparent said:

‘The selection of TMP was shrouded in secrecy and smacked of underhand dealings which we know happens whenever sole sourcing approach is used in procurement contract.’

He further explained that TMP was first contracted to prepare a business plan for the company but GT management was surprised when TMP was later asked to form a partnership to implement their own-designed business plan. There is a further suspicion coming from the



procurement officer and the selection of TMP as a partner was a foregone government decision. His basis was the manner the contract was advertised at a short notice. According to the procurement officer and also corroborated by other informants from GT, the government had placed an advertisement in the local media on April 9, 2002, with a deadline of April 30 for investors to respond. According to them reputable suppliers would need more than the short period stipulated in the contract to submit their bidding documents. GT interviewees therefore suspected that the government caused the contract to be advertised in order to satisfy World Bank's requirements for all its sponsored projects to be advertised for competitive bidding. The DCEO explained his views further:

‘There seems to be the feeling in my opinion that the contract awarding process was hastily done ‘If we look at the short period given for prospective bidders to submit their tender, it is obvious that the deadline was mean to cut off all other competitors, to the benefit of TMP.’

However, GOF1 disagreed with the idea that the tendering process was deliberately done to favour TMP. He explained that:

‘I agree that, TMP originally contracted under a memorandum of understanding to prepare a business plan to transform GT into a modern telecom company; but because no other company indicated its interest to compete, and TMP was confident of successfully executing its business plan, it was decided to awarded the contract to the company without further delay.’

The government officials explained in the absence of other rival bidders, the choice of TMP was also informed by the fact that the government found the business plan of TMP commercially sound and believed that the company has good appreciation of the Ghana

transactional environment and government's objective than any new supplier unfamiliar with the challenges facing the company.

Despite these divergent views on the question of transparency or otherwise, what was clear from the interviews was that GT had faced limited supplier competitive bidding for the telecommunications project which in turn, suggest that the bargaining process is not going to be an arm's-length bargaining. GOF1 admitted this and commented as follows:

'From hindsight, we now realised that we were at the mercy of TMP as the sole supplier...and our experience from the negotiation showed us that you cannot make any impact when negotiating with a single supplier.'

#### **7.1.4. Information on the contract**

This section presents the TMP interview responses to questions about information on the contract. Results of the interview on accessibility to the relevant information on the contract that affected their negotiation strategies were outlined.

As mentioned earlier in the Chapter 3 and Chapter 5, many accounts of power move beyond questions of scarcity and utility but also consider the relative information resources of the two parties as well (Cox et al., 2000). In negotiations, information is regarded as power and this was recognised by the interviewees. Interviewees noted that reliable information makes it easier for the authorities to plan, communicate and negotiate with the contractor on equal terms. They also mentioned the importance of information to the design and effective monitoring. Unfortunately, however, interviewees DCEO2, PO2, AD2 and EBM2 found this not to have been the case with TMP negotiation.

These interviewees catalogued key information gathering problems pertaining to the complexity of the transaction and the unco-operative attitude of the service provider regarding key information on their cost and mark-ups. An ex-board member (DCOE2) was particularly emphatic that GT had little or no strategic information about TMP these matters before the negotiation started:

‘I have my doubts the negotiation team had a full knowledge about the technical requirements of the telecom industry in the area of its costs estimates and mark ups.’

He further noted that:

‘Since we could not work out what efforts were involved in the management work and the methodology to value such efforts we could not challenge them effectively on their claims on the contract cost and salaries they requested. The information we had on TMP was basic on their line of business, financial viability and experience from their websites and our transaction advisers also sponsored by the World Bank.’

According him the government decision to sign the contract was based on the limited information given to them TMP because they did not have the time and resources to search for the needed information.

### **7.2.1 Supplier Side TMP**

This section presents the TMP interview responses to questions about their evaluation on the importance of the project to their businesses. On the question of utility of the GT project, it emerged that the transaction had lower operational and commercial value to them in relation to their market opportunities elsewhere.

Operational Importance: An interviewee representing TMP (ADO2) described the contract as desirable but not as operationally or commercially as important to them:

‘When we looked at the telecom contract and compared it to our main operations of the parent company, it did not serve as an important component part of our business offering to our existing market and customers... GT business was considered as another business opportunity we explored, but the loss of that contract would not have had any significant effect on the survivability of the parent company of Telenor Norway.’

He further explained that:

‘The TMP company was specifically formed and incorporated in Ghana, and all our staff who worked were posted here on secondment and after the contract ended went back to their posts in Norway.’

However, COF2, also representing TMP, provided a slightly different picture. He viewed the transaction as not equally important to them as to GT but admitted that the telecoms contract was central to their business objective of gaining a foothold in Africa:

‘From a purely business perspective, the transaction increases our business portfolio and presence in Africa; and we considered at that time by accepting the GT contract which was by standard low value it was going to give us advantage in winning future contracts in Africa.’

Commercial Importance: Similarly, from commercial point of view, it was evident that in terms of value and size, the telecoms contract was not materially significant. The Deputy CEO (DCEO) working with TMP and information from its websites the total volume of business and annual turnover of the parent company. The DCEO outlined the business profile of the company that had business dealing in a number of European countries. According to DCEO, in terms of value and size the winning or loss of the telecoms contract would not have affected the fortunes of the parent company.

In relation to information, it was evident from the interview that TMP was well informed than the GT. Manager EBM2 stated:

‘We shared every bit of information we think they should know at the negotiation but admitted that there could be some information that had to be kept private’.

Although, the interview could not obtain confirmation that the cost structures were openly made available to GT, responses indicated that the service provider had an advantage in the critical aspects of the transaction on what efforts were required on executing the contract and required returns they want for taking risk in the contract.

#### 7.2.2 Interview and Other Data: Negotiations and Resources and Capabilities

In this part, we assess the evidence relating to the second independent variable of resources and capabilities in negotiations within the argument being tested in this thesis. We begin the analyses by examining the relative resources and capabilities of both GT and TMP, in terms of their ability to communicate and negotiate effectively with each other, and on equal terms. This is followed by an analysis of their effect on the contract negotiations and design.

#### **7.2.3 The Negotiation Resources and Capability of GT and TMP**

This section presents the GT interview responses to questions about their evaluation on their commercial resources and capabilities.

Resource and Capability Asymmetry: Contract negotiations are always considered important in business exchanges: They set out precisely each party's obligations and responsibilities, risk and rewards. Since what a party gets out of a contract is based on the negotiate outcome, the conventional wisdom has been for companies to carefully choose their negotiation team, people with the requisite knowledge and skills to handle the demands posed by a particular transaction. Yet this appears not to have been the case in the telecoms contract; asymmetry of resources and capabilities between GT and TMP.

It emerged from the interviews that the negotiation team was made up of selected people from the Ministry of Finance to serve as an observer, a legal representative from the Attorney General department and three other government appointees. According to PO2, the negotiation team was headed by the Minister for Communication who exercised real authority when it came to approval and signing of the contract DCEO admitted that the selection was not based on professional knowledge in negotiation or proven experience in contract negotiations. DCEO further explained that:

‘The Minister who led the team had no record of experience in business negotiating, and the Ministry of Finance staff were included in the team for the reason that they would be handling the receipts and disbursement of funds under the contract.’

The explanation offered by a GT interviewee (GOF1), on the direct involvement of the government was that:

‘It is an established practice for the state to undertake negotiations, and sign on behalf of a public sector body when the value of the project has serious effect on the national budget. The Ministry of Finance is mandated by law to receive loans and its repayment on behalf of public sector bodies in the country’.

The findings suggest that the negotiation team, apart from its relative lack of experience and commercial skills did not act independently of government influence. The idea that the GT negotiation team's performance is routinely influenced by government political interests was also articulated by EBM2 who was part of the negotiation team. He stressed the point that government right to appoint negotiators is not the problem but it is the act of dictating to the team what to do is the issue with GT contract.

He conceded that the political authorities directly influences the contract negotiation whose directives difficult to refuse in Ghana. He noted that:

‘The political authorities and ministers tell you to award the contract against your professional judgement but you have no choice because you cannot defy the government authority in these matters. I must admit that the TMP had prepared the final contract document and then presented to us to approve within three days.’ Except the person from the attorney general department who had legal background, the rest of us found the language [in the contract document] confusing and difficult to understand...and we were asked to read through and approve it as it was.....and had to approve the contract the way it was without any amendment.’

He therefore explained that the problem of poor performance of the government negotiating team with the private sector was not because of poor training and experience but it was the because the political authorities interfered in the pre-contractual negotiations and dictated to the negotiation team to sign the contract.

PO2 also added that:

‘Because people with professional qualifications and knowledge were not selected, the negotiation team had no strategy to counter what the service providers threw at them... definitely our negotiation team was overwhelmed by the TMP team.’

In terms of specific ways in which the public sector negotiation team could be strengthened, interviewees from GT (PO2, AD2, and EBM2) admitted that this could be difficult in the case of international contracts but proposed that the procurement department should be empowered to handle future contracts. The procurement officer (PO2) emphasised this clearly:

‘Resourcing the procurement department in terms of professionally qualified staff, training and logistics and political support and allow the professionals to take decisions on behalf of the government.’

Overall, the general perception from the interviewees from the public sector (GT management and government) was that the government negotiation team did not perform well because they were ill-equipped to match the competency of the service provider.

### **7.3 Analysis of the Pre-contractual Power Relationship**

This section reviews the pre-contractual power variables from the interview data to assess whether the pre-contractual power relations was symmetrical, or asymmetrical for GT. Based on measurement constructs outlined in Chapter 5 the determinants of the pre-contractual power relations between the client and the service provider are the demand and supply characteristics of the transaction: i.e. utility, scarcity and information. As a test of this hypothesis, empirical analysis is from the interviews and documentary sources. In this section the empirical analysis presented here is to compare qualitatively the pre-contractual power resource of GT and TMP. The objective is to determine whether or not GT was in adverse pre-contractual power relations.



### **7.3.1 Pre-contractual Power Analysis:**

From a buyer's perspective utility of supplier's services refers to the use value of the item to its needs. The results of the interview displaced in Table 7.1 shows that the GT utility (operational and strategic importance) of the transaction was relatively higher than that of the supplier. It is the objective of the government's objective of opening up the country to local and foreign investors and also to raise the status of GT operations to international status. Additionally, the government wants to extend ICT to schools and colleges in order to equip young adult with basic computer skills before they leave school. Thus the government consider the service offerings as both strategic and operational importance to achieve these objectives.

From the supplier's side, utility refers to the attractiveness of the value of the transaction that increases its revenue or profits (Lonsdale, 2005a; Cox et al, 2001). The main consideration for TMP will be whether the telecoms contract value forms a higher percentage of its total revenue operations.

In comparison to TMP, Table 7.2 shows that the contract constitutes about 0.083% of Telenor Norway's total turnover. The annual turnover of Telenor Norway was over \$6.5 billion at the time of the transaction as compared to the GT contract value of \$5.4million. From commercial and operational perspective, given the low ratio of the telecoms transaction it is likely that TMP executives may not consider it as an attractive enough for them to divert resources towards securing the contract. At the utility level, it is evident that GT's utility is higher than the service provider.

**Table 7.1 Summary of Results: Pre-contractual Analysis of GT and TMP**

Buyer Power Resources (Indicators)	Supplier Power Resources (Indicators)	Buyer-supplier power structure
<p><u>Utility</u></p> <p>TMP transaction both operationally and strategically critical to government agenda: country's socio-economic development agenda. ICT to businesses and schools.</p> <p>Contract value forms less than 1% of TMP parent's total annual turnover. Limited volume of demand to leverage supply.</p>	<p>Supplier's services critical to GTs strategic and operational objectives</p> <p>Larger share of GT's business needs</p> <p>Lower transaction value to total business turnover.</p> <p>GT's transaction desirable but not of critical operational importance</p>	<p><u>Supplier dominance</u></p> <p>A&lt;B = TMP's leverage advantage</p>
<p><u>Scarcity</u></p> <p>i.No alternative suppliers.</p> <p>ii.Limited opportunities to stimulate bidding competition</p> <p>iii.Few suppliers available to take on management services with GT.</p> <p>iv.Cannot substitute or redefine telecoms transaction to increase options.</p> <p>v.Restrictions imposed by World Bank Conditions. Sovereign guarantees and Political risks</p>	<p>i.Lack of active interest from foreign companies to compete for the project.</p> <p>ii restricted by perceived political risk in the delivery of telecom services</p> <p>iii.Natural monopoly of telecom market: High entry barriers with few qualified suppliers.</p> <p>Non-substitutability of telecom services</p> <p>Wide business network and options available to develop business opportunities</p>	<p>A&lt;B = TMP's leverage advantage</p>
<p><u>Information</u></p> <p>Limited information on supplier's costs and returns.</p> <p>Limited information on supplier's management systems and performance</p>	<p>Information on project budget available.</p> <p>Keeping private information on cost and returns from GT</p>	<p>A&lt;B= TMP's leverage advantage</p> <p>Overall AVRL is dominant</p>

Key: A= Buyer Dominance  
B= Supplier Dominance  
C= independence  
D= Interdependence

In terms of scarcity, from buyers' side this refers to the number of potential or actual suppliers that could be obtained in a market for a particular transaction (Cox et al, 2001). If there are few suppliers in the market a buyer will have less leverage over price negotiations than if there are many suppliers engaging in competitive bidding. From the Table 7.2 and Table 7.3 we find that GT had only one supplier to select for the contract. The explanation given is that only one qualified supplier responded to the advertised contract suggesting that there were no potential suppliers to choose from in the market. In this case, the government has few opportunities to leverage the buyer and will be reacting to the only supplier available. By contrast, Table 7.2 shows that TMP has business opportunities to develop its business in other markets should the GT contract fail. A consideration TMP executives might consider is whether it is possible to obtain similar transaction elsewhere. Another possible consideration for the supplier would be to look beyond the current transaction into examining possibilities of future business with GT. If the future possibilities exist for future business are high, the typical supplier would consider the relationship as strategic value. In that case, GT will have opportunities to leverage the supplier for good deals. However, the present case does not appear fit into those circumstances. Analysis shows TMP's parent company Telenor Norway has extensive operations in 18 countries in Europe, South East Asia and North America. It is one of the world's largest suppliers of mobile satellite communications, and the world's third largest supplier of satellite services via the Inmarsat system (Telenor Norway, 2010). This implies that TMP will be indifference if it fails to win the telecoms contract. The reason is that utility of a transaction is related to other business opportunity that can be developed elsewhere as an opportunity cost. Given their extensive market and diversified business portfolio, it is logical to assume that the private sector company has many options in the market to develop its business reinforcing the conclusion that the contract may not be attractive to TMP. This gives TMP leverage over the Ghanaian government. The last key

power resource that structure pre-contractual bargaining positions are information. Results reported in Table 7.2 and 7.3 show that the TMP is better informed than GT in terms of contract pricing and margins.

**Table 7.2 summary of Findings for TMP (Supplier)**

Supplier TMP	
<p>Operationally: telecoms contract considered as an additional investments; Transaction not considered as key account Contract serving as a stepping stone for GT to enter the African sub-region Commercially: telecoms contract value ratio to total Turnover is 0.083%.</p> <p>Buyer Scarcity</p> <p>The consortium operates in other markets in Europe, South East Asia and North America. Opportunities to develop further markets. The transaction could be replaced with a better contract value</p> <p>Information</p> <p>Supplier had full access to GT project budget information about what TMP wants from the transaction From World Bank websites, Ghanaian public officials, Ghana websites. Past experience, industry wide pricing formula</p>	<p>Low percept to Total Business turnover</p> <p>Got options in other markets.</p> <p>Could easily replace GT contract with a high value/volume contract</p> <p>Informed about the project budget and mode of financing.</p> <p>Private information on how much the Ghana government prepared to pay</p> <p>High information</p>

TMP obtained information from the World Bank website and tender documents with prior knowledge about the budget for the contract and possibly how much GT is willing to offer.

By contrast, GT officials had limited information on the lowest price the service provider is prepare to accept. We found no evidence from the interviewees on GT side that TMP shared private information on cost schedules for the project with GT officials.

Meanwhile, information asymmetry on the part of the government may make it difficult for the government to cross-check whether cost and mark ups of GT are genuine and reasonable. From this perspective, TMP has bargaining advantage over the government in terms of price.

**Table 7.3 Summary of Findings for GT Interviews**

Buyer (GT)	Suppliers (TMP)
<p>Utility</p> <p>Operational: The contract with GT critical to the continued operations of the company.</p> <p>Importance: To support foreign investment drive; Key to economic recovery agenda. To extend and increase telephone density; introduction of broadband internet penetration</p> <p>ICT development in schools and universities. To support government computerisation of services and e-commerce</p> <p>TMP transaction: linked to World Bank financing support.</p> <p>Scarcity: sole sourcing; Only TMP submitted a bid.</p> <p>Telecoms market structural barriers: no competitive bidding</p> <p>Non-substitutability: No alternatives to fulfil the same function</p> <p>Information;</p> <p>The negotiation team had limited information on the minimum price acceptable to suppliers. Limited information on supplier's cost and rate of return.</p>	<p>Utility high</p> <p>Transactional salience</p> <p>Supplier scarcity</p> <p>Information asymmetry</p>

The above analysis shown in Table 7.1 clearly shows that the utility of the TMP offerings is higher to the Ghanaian government than it is to TMP operational and commercial needs. In terms of scarcity, it is evident that GT faced limited choice in supplier selection. Some factors like entry barriers and the difficulty of getting alternative suppliers indicate that TMP is irreplaceable, at least, in the short term and may account for some difficulties of GT. Furthermore, TMP is better informed about key issues of price and costs of the transaction whilst TMP had little information on how much value TMP has placed on the contract,

therefor is not in position to challenge TMP proposals. From this consideration, GT is likely to have less bargain power to leverage TMP. In combining the three power resource variables of utility, scarcity and information we can reasonably conclude that GT may found itself in a weaker bargaining position with TMP.

Despite the above analysis, it is important also to observe that suppliers may not fully disclose their high utility in a particular transaction for commercial reasons, to the buyer. This question came up during the interview and the DCEO2 was hesitant to make definite stand on actual commercial or operational importance to TMP. Therefore there is a possibility that, although analysis suggests that the telecoms contract is relatively attractive to the GT, there is possibility that TMP considers the telecoms contract equally high.

### **7.3.2 Analysis of Factors Resource and Negotiation Capabilities**

This section uses the evidence from the interviews to evaluate the potential existence of resource and capability asymmetry negotiations between GT and TMP. The primary hypothesis predicted that asymmetry in resource and capability will impact on the ability of public sector manager to design a balanced contract. Interview data was collected from both GT and TMP executives Findings showed that the resources and capabilities between the government and TMP negotiation teams is asymmetrical in favour of the service provider.

To establish that an asymmetry exist between the GT and TMP, key indicators were negotiators experience, commercial knowledge, technical competence and independence in

taking the contract decisions were obtained and compared. Using the metrics we designed in Chapter 5 results showed that there was indeed asymmetry between the GT negotiation team and the TMP representatives.

Results in Table 7.4 and 7.5 show the composition of the both GT and TMP negotiation teams.

**Table 7.4 Summary of Interviews on Negotiation Resources and Capabilities**

Indicators	GT	TMP
Composition	Adhoc negotiation teams ie each from Ministry of Finance and Economic Planning and Attorney General Depts. Technical Director of GT and a minister of state.	Sales and marketing department Mr. Illiamson expert and head of Contract Negotiation and two others from sales department.
Experience	Negotiation team had no previous engagement in similar transaction	Negotiation team has engaged in similar contract negotiation elsewhere
Skills	Exhibited low commercial and understanding of the transaction. Did not conduct project economic analysis	Exhibited profound sound commercial understanding, analysis and technical understanding of project requirements
Independence	Team was prevailed upon to accept the contract terms	Team was independent and applied professional judgement in line with organisation's objective
Deployment of	Unable to challenge supplier's contract proposals	Able to push their proposals as against GT's team strategies

The GT negotiation team is made up of representatives each from GT (technical side) Ministry of Finance as a witness and a representative from the Attorney General's department. From this composition, it is evident that none of the GT's team has any strong procurement background. We note that whilst the GT's negotiation team is composed of selected individuals with little or no commercial skills or experience, TMP team is made of individuals with sufficient knowledge in commercials and past negotiation experience. It could also be infer from the display from the table that GT appeared to view the bargaining process as given and may have not planned adequately towards it. Or it is also possible that

they trusted the service provider and did not see the need to subject TMP to strict arm's-length contractual bargaining.

**Table 7.5 Mapping the Resources and Capabilities of Negotiations**

Indicators	GT	TMP	Symmetry/ Asymmetry
		Sales and Marketing Department	asymmetry
Professional qualification	No member of procurement background was included in the negotiation team	.Strong indications but details not made available.	asymmetry
Technical knowledge of the project	Yes. One Technical Director included.	The three member negotiation team had strong background in contract negotiations Used their technical staff and project/ investment appraisal staff.	symmetry
Previous experience	None of the members had prior experience in similar transaction	The three member team had previous in contract negotiations in other countries.	asymmetry
Commercial knowledge /skills	None of the members had strong commercial knowledge in negotiations	Obtained from training and experience	asymmetry
Independence	Members appointed by government: reliance on government directives.	Independence and professional judgement	asymmetry

By contrast, the supplier side's perspective on the contract is quite different. TMP appeared to have full idea of what they want from the telecoms contract and the understood the importance of securing good contract to maximise their returns through the contract design by presenting a strong negotiation team. The leader of the TMP, Mr. Illamson is described as forceful negotiator who had built a reputation as someone who does not give away concessions often, or compromise on it in past negotiation activities in Europe (COP2; ADO2). This implies that the team negotiating on behalf of GT came up against a tough negotiator The Corporate Affairs of the company explained that TMP followed a standard



procedure of approaching any contract negotiations from a purely business point of view and this is reflected by the way nothing was left for chance by selecting a seasoned negotiator to negotiate with the government.

The superiority of TMP over GT team is made more evident during the negotiation process. We found that the contract document was drafted by the service provider and presented to the GT side. The contract terms was approved without subjecting them to intense scrutiny and negotiations. This can be interpreted in one of two ways. Either the GT team lacked basic commercial knowledge and experience to challenge supplier's proposals or they trusted the TMP to be honest in the drafting of the terms and conditions. Given that the TMP negotiation team singlehandedly designed the contract document, two possibilities could be pointed out. Firstly, TMP negotiation team may have craft favourable terms for itself. Given the background of the members TMP's negotiation it is reasonable to expect their project appraisal team to be able to identify the general and specific risk in the industry. Secondly, GT signed the contract containing supplier's traps that will be used to hold GT in the relation. Given that the TMP is looking for opportunities to design good terms, it is reasonable to assume that the public sector might have been outwitted. Despite this analysis, we find that the relationship between the variable negotiation resources and capabilities and contractual imbalance in the relation weak.

### **7.3.3. Conclusion**

The pre-contractual power analysis showed that the supplier has a favourable bargaining power in the relationship. Firstly, the utility in the supplier's offerings is found to be higher

than the commercial attractiveness of GT transaction to TMP. Secondly, TMP was irreplaceable as a result of lack of equal qualified suppliers in the industry. Finally, TMP is better informed about the critical information about cost and returns than GT.

With regards to the second independent variable of resources and negotiation capabilities, TMP raised a superior negotiation team and dominated the negotiation proceedings. However, we find that the relations between the second independent variable and the hold-up that occurred as weak.

In the next section, we investigate whether or not the contract was balanced in terms of risk sharing and uncertainty and if the adverse pre-contractual power relations can explain it.

#### **7.4 Analysis Post-Contractual Imbalance**

The main aim of this section is to analyse from the empirical data whether there is evidence of post-contractual balance between GT and TMP. The first hypothesis is that adverse pre-contractual power relations on the part of the public sector will make it difficult for the government to achieve post-contractual balance. In other words, adverse pre-contractual power relations lead to post-contractual imbalance. Consistent with the proxies in our methodology chapter for the measurement of post-contractual balance, our analysis focuses on whether:

- i) The terms and conditions of the contract exhibit a fair representation of what each party in the relationship expects and do not impose onerous obligations on one party and not the other.
- ii) Underlying specific assets were equitably shared, or in the absence of that, financial hostages were posted.
- iii) The contract design integrates the necessary incentive structures and self-enforcement agreements with the necessary incentive structures i.e. postings of ‘financial bonds’ to sustain mutually inter-dependent relations post-contractually.
- iv) There was open sharing of information and transparency (open book system).

The analysis is conducted based on the results of the study of the telecom contract, in order to evaluate from the case whether or not post-contractual balance occurred. There are, many issues in the contract suggest that risk and uncertainty were not shared equally in terms of transaction-specific investments, incentive contracting, inflexibility and information sharing. We will examine these in detail.

#### **7.4.1 Risk Sharing: Fixed Assets**

The analysis in this section evaluates the data collected from the PPP-run telecoms contract. The objective of the empirical analysis presented here is to investigate whether adverse pre-contractual power relations of the GT created post-contractual imbalance. Typical standard TCE theory dictates that the public sector should share risk and uncertainty in relation to the private sector when the relationship is supported by transaction-specific assets (Williamson, 1983; UK Treasury, 1995). In PPP, it is argued that if risk and uncertainty in a relationship

are not shared equitably with the private sector, the public sector will find itself locked into the transaction and contractual dependency.

According to the contract terms, GT was responsible for the provision of investments into the infrastructure and rehabilitation and the purchase of new equipment. Thus the contract excludes TMP from contributing to the transaction-specific investments in GT. The explanation from GT during the interview was that even though they made efforts to encourage any incoming partner to invest in the company's infrastructure, suppliers were not interested in taking up risk in the company. On the supplier side, it became evident during the research that TMP were concerned about the potential risk in investing in the telecoms company. The other possible reason for TMP decision is that if the incoming partner does not see the need to work collaboratively with the government for a long time will not divert its resources to develop the relationship. In the previous section, we notice that GT's transaction is of low volume to its strategic needs and the three year contract with no possibilities of further extension might have influenced the decision not to accept risk in the relation.

From TMP's perspective, although the management saw the need to jointly invest in the relation, probably considered the risk in the relationship and the uncertainty regarding the telecoms operations and government's behaviour to be high and thought it appropriate for the government to manage its own risk i.e. infrastructure investments, tariff policy and debt collection. GT on its part, decided to take the risk since it seems GT had difficulty in getting TMP to accept risk. Given the non-availability of alternative suppliers, two choices faced GT to get TMP to agree to form the management partnership- through inducement or accepting TMP's terms. Analysis showed that GT was forced to take up all the risk of the telecoms

infrastructure investment costs in order to get TMP to enter into the partnership. This placed TMP in a dominant position.

#### **7.4.2 Risk Sharing in the Contract: Cost Plus Incentives**

In the incentive contracting literature, there are three common ways of pricing a contract: fixed contract fees; fixed contract plus costs fees; and variable pricing plan (Weitzman, 1980; Laffront and Tirole, 1993). With the fixed contract pricing plan, the service provider receives fixed revenue to execute the contract. The advantage to the buyer is that the risk and uncertainty in the relationship are passed to the buyer to manage. From the perspective of economic efficiency, the supplier bears the cost uncertainty and that provides a strong incentive for the adoption of cost-effective means to minimise cost and maximise profit (see Weitzman, 1980; Mcfee and Macmilan 1986; Laffront and Tirole, 1993). The only drawback for the buyer side is that such a contract price includes a risk premium to account for uncertainties.

The other more flexible plan is the variable contract, which ties payment to the units of service or product produced, with bonus systems. This is the best pricing plan for the buyer, as it involves sharing risk and uncertainty with supplier. Another advantage is that it allows parties to quickly adapt to work out any problem to reduce costs.

The alternative pricing plan is the cost plus pricing plan. In this pricing plan the supplier, is reimbursed for all expenses incurred, in addition to the fixed revenues. This means that the buyer effectively insures the supplier against all cost uncertainty. Since all cost inefficiencies are reimbursed, the supplier is not motivated to be efficient in delivering good value for money. On the buyer side, the choice of contract plan will be the one that makes the supplier take the risk and uncertainty, which is the variable contract price. On the supplier side, the pricing plan guarantees its income and cost refunds which is to say that the buyer takes on all risk and uncertainty in the relation.

In brief, commercial sense dictates that the buyer will choose variable contract price where risk and uncertainty is passed on the supplier if it is in power dominance. On the other hand the supplier will choose fixed cost plus pricing plan when it is in dominance a situation that makes it possible to pass risk and uncertainty to the buyer. This contrasting preference scenario allows us to determine who has the power to make the other party to accept their contract pricing plan.

The telecom industry is a service industry and the complexity of its operations means that considerable risk and uncertainties characterise its operational and commercial outcomes. Revenues depend on subscriptions and the level of expenditure subscribers are willing to make in a month. This, in turn, may be affected by levels of disposable income of subscribers. In a developing country like Ghana with low incomes, it is difficult to determine sales levels at any given time. Similar uncertainties affect cost. This is particularly the case because telecoms operations are subject to political interventions in terms of tariff policies,

foreign currency fluctuations and financing cost of infrastructure and equipment, none of which can be predicted with reasonable accuracy for investment decisions.

A potential risk in the relation is political risk. Concerns over political risk in developing countries means that foreign companies avoid taking on risk and uncertainty if they are to accept working in collaboration with the government. From TMP's perspective, the combination of these factors may mean that the telecoms contract is characterised with high risk. From business point of view, and in order to protect its investments and maximises its returns, the TMP will take less risk in the relation by choosing cost plus fixed contract. The service provider can only do that when it is in dominance

On the buyer side, it is appreciated that in a management contract the operational and commercial performance of the project depends on the efficiency of the agent. A contracting party is confronted with uncertainty if the contracting party cannot know beforehand the level of effort required to perform a particular task. The same uncertainty pertains when the track record of the agent is not known raising a probability of moral hazards (Holstrom, 1979; Eisenhardt. 1989. To the management of GT, this aspect of the relation poses considerable risk because of lack of information on the kind of value adding activities that the service provider should employ to achieve cost savings and functionality Given the concern for moral hazards, two options are open to a contracting party ie GT. First option is to take on less risk and transfer more of it to the private service provider. The other option is use risk-incentive trade-offs in the contract design. That means using variable contract price plan. This form of contract design allows the government to achieve its strategic objectives of providing essential telecoms services to the people, and at the same time allows the service

provider to make reasonable returns on its services. However, this strategic move will get the supplier to take some risk which the service provider if he in dominance will resist.

Analysis showed that the service provider is receiving its revenues under cost plus plan. The signing of fixed cost plus contract has the implication that it reduces the uncertainty in the transaction for TMP. However, fixed contract price can be risky for TMP in case revenues from GT operation increases beyond budgeted. In that case, GT will lose possible future net contributions from accepting fixed instead of variable and fixed guarantee income. It appears that TMP achieved this purpose by its exclusivity access to revenues cost disbursements in the company. The exclusive control of the GT accounts is confirmed during the interviews (DOO2; AD2; EBM2) and also with supporting evidence from the Ministerial Report that investigated the sale of GT to UK Vodaphone (Inter Ministerial Review Committee Report, 2009). The evidence that cost plus contract is chosen and the fact that the service provider strategically avoided in contributing to the dedicated assets presupposes provide indication that risk sharing is not balanced. In other words, the ability to force the government to take up all risk upfront suggests that TMP is the dominant party and also has significant leverage over the government.

#### **7.4.3 Sovereign Guarantees and Switching Costs.**

TCE logic provides that the party, whose investments are at risk, in this case the government, should demand from the other party credible commitment in the form of financial bond to mitigate the risk. We find no evidence TMP was made to post any financial hostages. Instead, we found that the government was forced into providing financial bond instrument in the



form of government sovereign guarantee. A sovereign guarantee is a form of a promissory financial commitment issued by a state used as collateral that entitles the holder to enforce contractual commitment against state opportunism or unlawful contract termination (Hall, 2003; Mosley et al., 2004; Johnson, 2005).

Although the rationale for demanding sovereign guarantee is meant to increase contractual predictability of the governments behaviour over the contract period, international suppliers take advantage of that to create switching costs for the government. Since sovereign guarantees put a country's all assets including airlines, ships, buildings and any other sovereign state movable and immovable assets on the stake (high switching cost) governments seldom issued it unless it is compelled to do so. Given that the supplier forced the government to issue one and without the ability to demand similar financial bond from the service provider suggest that the relationship is not a balanced one. Given the little opportunities to leverage the supplier, it seems reasonable to expect the government to have less power to force the service provider to post the appropriate financial hostages to balance.

#### **7.4.4 Contract Inflexibility and Post-Contractual-renegotiation**

One major indicator that the telecoms contract might not be one of balance is related to contract flexibility regarding future events. In long term contracts, the parties may not know how future events are going to shape the relationship. As a result, parties to an exchange make provisions for future renegotiations when found necessary to restore the original integrity of the contract. If parties are in genuine power balance, they are able to adjust mutually post-contractually.

In the GT and TMP contract, we notice that the contract provision was rigid and inflexible towards the government. While the TMP could initiate steps on its own to re-open negotiations, GT on its part need to seek the service provider's approval. The problem with this arrangement is that service provider reserves the right to refuse contract variations or to more crucially to block any renegotiation except on its own terms. This could be described as one-sided contract arrangements in favour of TMP. This is made evident when the government made an attempt to re-negotiate the original terms with TMP executives regarding salaries paid to the expatriates which was considered to be on the high side.

The salaries and allowances paid to TMP and their executive management totalled \$300,000 tax free a month and paid direct from the GT accounts. When the salaries became public knowledge, the public was enraged over what they considered 'excessive' salaries and fat bonuses paid to TMP executives. As a consequence, the government came under pressure from the civil society and the press to renegotiate the salaries paid to TMP executives (Public Agenda, 2004; Insight, 2004). A subsequent government attempt to re-open negotiation to review salaries failed partly, because it was met with a credible threat of withdrawal from the partnership (DCEO2; DA2) and partly because the government did not want to take this path because any disputes have the potential to disrupt the services of GT.

Perhaps the major reason for abandoning the idea is specifically to do with the Malaysian Telecom contract termination that cost the government both financially and politically (Haggartey et al., 2002), which were fresh in the minds of the government officials. Moreover, it is the same government involved on the Malaysian Telecom compensation saga is handling the current TMP case. Thus it is reasonable to link the two cases and conclude

that threats of contract termination and possible compensation payments may have influenced the government's decision not to pursue the case.

It should be pointed out that Ghana's government's attempts to change the salaries failed for some other reason. Instead of seeking changes to the salaries levels, the government should rather be seeking to increase service delivery in return for increased fees. This indirect approach would have been more acceptable to the service provider (see Bajari and Tadelis, 2002). However, it comes back to the same point of its weak power position vis-a-vis the service provider.

#### **7.4.5 Information and Moral Hazards:**

Information sharing and transparency are at the heart of agency partnerships (Pollock et al., 1999; Eisenhardt, 1989; Holstrom, 1979). However, it appears that information sharing in the telecoms contract was problematic. Analysis suggests that TMP's relationship with GT was characterised by a high level of information asymmetry. Some interviewees from the GT side (DCEO2; DA2; HRM2) explained that they received irregular reports and critical information was selectively released by TMP. One of the executives (DA2) further explained that the information gap was high, but traced the problem to the fact that the three top offices of Chief Executive Officer, Head of Finance/ Administration and Head of Technical were occupied by TMP executives. Given the positions held by the service provider, it is natural that all operational and commercial decisions were taken by them. The technical auditor appointed to examine the accounts gained access once a year at the year end.

Further investigation revealed that whilst the local staff cooperated with the service provider by sharing important information about the company's operations, TMP executives hardly exchanged any information, particularly on the basis on which expenses were incurred on behalf of GT (DA2. Meanwhile, the lack of access to key information was affecting the work of the GT management, but they could not do anything about it, which further suggests IT weak power position with TMP.

Evidence in the case also showed that the supplier controlled information flow and took every opportunity to deny GT management to the books. Not only did TMP executives selectively made information about revenues and costs but also frustrated genuine GT management's attempt to secure a bank loan of \$200million to support GT operations (see Inter Ministerial Review Committee Report, 2009). There is further evidence that showed that TMP is dominant when it comes to financial decisions in the relationship. The CEO of TMP applied for and took out an overdraft facility of about US\$5.5million from Ghana Commercial Bank Ltd without seeking clearance from GT board (Inter-Ministerial Review Committee Report, 2009: 21, paragraphs 35&36). In both instances the service provider got away with without the government applying sanctions (Inter Ministerial Review Committee Report, 2009). The government have not got sufficient power resources to control the behaviour of the service provider indicating that the power balance is in favour of the supplier.

In summary, and based on the above analysis, there is sufficient evidence to suggest that GT is in post-contractual imbalance with TMP. Firstly, TMP did not contribute to the dedicated assets; the contractual terms were skewed towards TMP. Secondly, TMP chose incentive contract pricing as a fixed contract price plan with scope for cost disbursements, thus leading

it to take on little or none of the risks and uncertainty in the relation the service provider. Thirdly, the service provider hardly shared any critical information on how it is operating the accounts. In effect, the relationship between the government and TMP can be classified as adversarial in favour of the service provider. In combination, and based on the weakness of the government to force the service provider to operate an open book system, one can reasonably conclude that the Ghanaian government is in adverse post-contractual balance with TMP.

Having first established that the post-contractual balance was in favour of TMP, we proceed to examine whether this was caused by the adverse pre-contractual power relations. The first hypothesis is that the adverse pre-contractual position of the public sector organisation will make it difficult for it to develop post-contractual balance. In making this analysis, we could examine the agreement itself, but in this specific instance we are interested in the level of relative power of each of the parties before the agreement is signed, and how that impacted on the design of the contract. The rationale behind this approach will enable us to determine which of the two parties was in a favourable pre-contractual power relation to dictate the terms of the contract to his benefits. This brings us to the power theories earlier discussed that the party who enjoys favourable pre-contractual bargaining power dictates the terms of contract. From the Emersion (1962) power and dependency model and power regime model (Cox et, al., 2000), the dominant party will force the weaker party to take more risk at the contract design stage, The results from our earlier analysis on pre-contractual power relations in Section 7.3.1 which showed that the GT enjoyed favourable pre-contractual power relations significantly contributed to the weak power position for the government. Predictions from the resource dependency theory hold that the party that enjoys favourable pre-contractual bargaining power dictates the terms of contract under which it is prepared to co-

operate (Cox et al., 2001; Emerson, 1962). The implication is that TMP's ability to force the government to take more of the risks and manage the relationship uncertainty, while it retained little or no risk. Based on the above considerations we can assume that the service provider took advantage of its pre-contractual power position to design a contract that maximised its returns while taking less risk and uncertainty in the relationship.

From GT's perspective, the public sector company may have accepted the terms of the TMP for a number of reasons. Firstly, the telecoms transaction is of relative importance to the government's social and economic objectives and it was keen to form the collaborative relationship with TMP. Secondly, in order to get the service provider to agree to the collaborative relationship in running GT's operations, it had to take on the risk and uncertainty upfront. Thus it appears that adverse pre-contractual bargaining power (as defined by utility, uncertainty and information), and to some extent asymmetry in resource negotiation, contributed significantly to the inability of the GT to develop post-contractual balance with the TMP. The government's pre-contractual bargaining is made worse by its negotiation team unable to subject the proposed contract terms and conditions to strict scrutiny and the loopholes created a legal enforcement which the service provider could exploit to hold the government in the relation.

Based on the above analysis, it is reasonable to conclude that the adverse pre-contractual power relations position of the Ghanaian government significantly contributed to the adverse post-contractual relationship balance with TMP. An important observation can be made concerning this conclusion. It may not always be the case that adverse pre-contractual power exclusively caused adverse post-contractual balance. Other factors may be present apart from

the variables analysed in this study. Therefore it is difficult to conclude from the limited available information that the contractual imbalance (hold up) that occurred was exclusively, as a result from the adverse pre-contractual bargaining power. With the same reasoning, if a buyer is in an adverse pre-contractual relationship, it does not necessarily mean that a hold-up has occurred or the buyer is in an adversarial relationship. For this reason we examine whether the adverse post-contractual balance of GWCL had any impact on supplier performance in the next chapter.

#### **7.4.6 Conclusion**

To conclude, this section presented the interview data and also analysed the power structure and found that the government was in adverse post-contractual balance. Analysis from the case shows that this adverse pre-contractual power relation contributed significantly to the post-contractual imbalance with TMP. In order to maximise its returns, TMP needs strong backing power to consolidate its structural power in the relation. This appeared to have been achieved through three strategies of creating high switching cost for the government through sovereign guarantee and rigid contract that virtually leaves no option for government to renegotiate the contract terms. Information asymmetry seems to reinforce this power positioning of the TMP. In this circumstance the supplier put the government under a state of dependency. Based on the evidence analysed, the first hypothesis is supported. In the next section, we examine whether the adverse pre-contractual balance of the Ghanaian public sector in the water contract had an impact on the level of supplier performance and post-contractual balance.

## **PART B:**

### **The Water Contract: Presentation of Data**

#### **7.5.1 Independent Variables : Pre-Contractual Data**

This section presents the interview and follows similar pattern as in the first case. Discussions on the pre-contractual power resources presented in two parts. The first part concentrated on the key pre-contractual variables of utility, scarcity and information, while the second part deals with factors that had indirect influence on pre-contractual power relation. Consistent with the pattern set in the first case the main interview was preceded by confirming from interviewees that the telecom contract contains significant asset specific investments and switching costs. When this was confirmed the interview proceeded to gather evidence of pre-contractual power resources from the interviewees.

The interview started by interviewing GWCL staff first. All interviewees from both public and private sectors were asked about the same question about the problems that triggered the need to bring in a private service provider to manage the water supply on behalf GWCL. Generally, the perception was that inadequate infrastructure, poor financial performance and inadequacy of water supply in the urban areas and the need to introduce improvement in service delivery was the key driver for the partnership. Infrastructure needs were identified in terms of water treatment plants, distribution pipes and technical needs. A government



minister (GOF1) who was interviewed provided government's justification on why continuation of water supplies under AVRL was central to the realisation of its mandate to the people:

‘Water is life and we have to do all that is possible to ensure everybody gets access to water. It was the responsibility of government to make water accessible to everyone, and we believed that our partner AVRL was supporting us to achieve our objective.’

On the question of operational importance, it emerged that the operations of GWCL had almost come to a halt at the time the contract was agreed with AVRL. The managing director of GWCL (DCEO) explained that:

‘Our basic infrastructure to support continuous supply of water to the people had deteriorated to the extent that most communities in the urban areas went for days without getting water. In other cities like Tamale, Koforidua and Cape Coast the situation was worse. Our water treatment plants had either broken down or could not cope with demand. All governmental interventions with its little budgetary support were not enough to change our water systems. AVRL came to our rescue at a time the GWCL was struggling to keep its water production and distribution to the urban centres going.’

**Strategic Importance:** Concerning the strategic importance of the water contract to the government, two factors stood out as most significant. First, as already mentioned, the government was pushed by the demands of its people for a reliable, accessible water supply. As government minister, GOF1 reiterated the responsibility of the government to satisfy the people with reliable water but this objective cannot be achieved without external funding and proper management. The search for external funding led the government to consider the private sector participation idea the World Bank had been proposing. The strategic importance of AVRL was summarised by the minister in charge of Water Resources Works and Housing (GOF2) as follows:

‘AVRL expertise helped the government to achieve its social goals in the provision of potable water and in support of health and sanitation programmes under the World Health Organisation and nothing could have been achieved, even modestly, at this stage.’

### **7.5.2 Scarcity: Supplier Availability**

This section presents the GT interview responses to questions about their evaluation on the relative scarcity/options. With regards to scarcity, two distinct problems stood out – lack of competitive bidding and limited supplier market from structural entry barriers were the major reasons the government failed to simulate competitive bidding. GOF1 explained that:

‘Although GWCL put out a tender in the newspapers inviting bids, the response was disappointing with three companies showing their indication of interest in the project.’

GOF1 further explained that between 2002 and 2005, global events particularly, financial losses in some Latin American countries, led to the collapse of water privatisation as leading water companies were reluctant to undertake investment activities worldwide. The effect was that most of the international water companies reduced their investment portfolios in other third world countries like Ghana. From these global events, GOF1 explained that the few suppliers within the industry reacted by reducing their investment portfolios. He said:

‘ Even the established water companies, such as Vivendi or Saur, reacted to these events by changing their corporate objectives, and investing only in large scale water projects with guaranteed profits.’

The other reason given for low supplier availability was the limited supply market and structural barriers to entry to the water industry. Three interviewees (DCEO, GOF2), agreed

that the supply market for water management services was limited to few suppliers and described them as difficult to attract for the urban water contract. GOF2 stated that:

‘Our search from the international market showed that only few foreign companies have the expertise to manage water systems in developing countries and this limited our choice because our contract was considered unattractive.’

Some interviewees also mentioned lack of local private sector capacity. GOF1 whose sector is charged with private sector development in the country observed that no local private company in Ghana had the financial and managerial capability to participate and win contracts with foreign companies. He revealed that:

‘Only one local company submitted its bidding documents but voluntarily withdrew its bid with the reason that it has not resources to compete successfully for the contract.’

He further pointed out that the major constraints on local private sector development are both financial and technical capabilities which his department is focused on addressing.

Another important factor which some interviewees (e.g., DCEO and GOF2) believed had limited the government’s choice was simply that of time. According to DCEO and GOF2, the water project had been delayed for far too long. To ensure its early implementation, the government had to award the contract to AVRL as quickly as possible when it became clear that no other supplier had submitted its bids to compete with AVRL. The DCEO expressed the desperate situation of the company as follows:

‘The water systems rehabilitation project had been delayed for 4 years, whilst we continued to run losses almost to the point that our water production level had dropped below fifty per cent. It was a question of getting AVRL on board as quickly as we can or we faced the prospect of total shutdown of our operations.’

GWCL management also faced additional problem. Political risks and economic uncertainty in many developing countries means that foreign suppliers were reluctant to invest in public sector projects in Ghana.

ADO1 further explained the challenge the government faced when searching for a willing partner from the supply market was frustrated by reluctance of the foreign companies to take up financing risks through build operate and transfer or lease models. As a result of this problem the government finally settled on AVRL, the only supplier out of the three companies who initially showed interest. In explaining the lack of interests from other two companies, he said:

‘The Saur’s management did not consider the contract price to be attractive and BiWater withdrew its bid very quickly, before it even reached the pre-selection stage.’ The government was left with little choice in the matter than to negotiate with the only company we have .’

The thrust of the interviews is that the government of Ghana found itself stuck with the supplier AVRL and this may have implications on pricing and contract terms.

### **7.5.3 Information on the contract**

This section presents the AVRL interview responses to questions about information on the contract. Results of the interview on accessibility to the relevant information on the contract that affected their negotiation strategies were outlined.

Similar to the telecom case, interviewees were of the view that GWCL approached the water contract with limited information on key aspects of the transaction. When interviewees were

asked about constraints on effective negotiations, DHR1, HRM1 and ADO1 noted access to information as being critical; but the latter observed that:

‘We had little information about how much profit the service providers earned on the contract and the methodology and assumptions that went into the fixing the contract price.’ This could have resulted in GWCL misunderstanding the consequences of the contract it signed with AVRL.

In contrast, the supplier appeared to be well informed about the water contract and about the key needs of the GWCL. According to HRM1, AVRL undertook a detailed audit of GWCL operations, and identified the key nature of the problems which affect supply of water in the country. They also relied on independent reports from the World Bank, and commissioned from independent project assessors. Therefore, it is evident from AVRL interviewees that they were better informed about the key aspects of the transaction than their GWCL counterparts.

#### **7.5.4 Supplier side: Utility**

This section presents the supplier’s interview responses to questions to assess the utility of the transaction to their operational needs and commercial objectives. From the supplier side, evidence was collected on the utility and scarcity pertaining to the water contract. This resulted in a picture, indicating that the GWCL water contract was neither operationally nor commercially important to AVRL. According to the CEO, the company’s overall business objectives and operations take place outside Ghana, which did not necessarily impact on how it continued to offer services to existing clients in the countries where it permanently operates. This point was underscored by DOA1:

‘We were impressed by the enthusiasm of the Ghana government to work with us on this water project in Ghana and we did accept their offer, but its effect on our continued services to our existing clients was not significant.’

On the question as to whether the loss of the water contract would have significant impact on their financial position, the CEO was emphatic that though they will be disappointed to miss the contract but its impact on the company’s finances will be minimal and pointed out the numerous business operations spread over several countries.

### **7.5.6 Summary**

This section presented the interview data obtained from GWCL-AVRL using semi-structured interviews. Interviewees from the public sector were unanimous in their assessment that the water contract was of strategic importance to the government. Interviewees also believed that the government faced supplier scarcity but believed that the whole negotiation process was particularly flouted in the award of the contract to AVRL. The interviewees also mentioned about the lack of information about key areas of costs and pricing and relied on the estimates from the service provider. In contrast, the service provider responses also indicate that the transaction was important to them, just that it was not critical to the survival of the company.

All these variables created adverse pre-contractual power relations for the public sector and consequently affect the governance design.

Some interviewees believed that the World Bank played a leading role in the weak bargaining position of GWCL. It was commonly pointed out during the interview that the World Bank’s pressure on the government to work with the private sector caused a shift in the bargaining power in the supplier’s favour. From the World Bank perspective, their role seems to be

neutral in coordinating the partnership between the government and the service provider without interfering in their affairs. The World Bank rejected the suggestion that their insistent of transparency in the award of contracts specifically in the Ghana water case can be described as putting the government in weak bargaining position. The interview results also showed that the government was made to provide insurance to the foreign company and that worsened both pre-contractual negotiation and post-contractual negotiations (GOF1 and GOF2).

## **7. 6 Analysis of the Pre-contractual Power Relation between GWCL and AVRL**

This section reviews the pre-contractual power variables from the interview data to assess whether the pre-contractual power relations was symmetrical, or asymmetrical for GWCL. Based on measurement constructs outlined in Chapter 5, the determinants of the pre-contractual power relations between the client and the service provider are the demand and supply characteristics of the transaction- utility, scarcity and information. In this section, the empirical analysis presented is to compare qualitatively the pre-contractual power resource of GWCL and AVRL with the objective to determine whether or not GWCL was in adverse pre-contractual power relations. The analysis is done based on the interview data and other documentary evidence summarized in Table 7.6. The analysis leads to the conclusion that the government was in a weak pre-contractual bargaining position with the AVRL.

Table 7.6 shows that the GWCL utility (operational and strategic importance) of the transaction was relatively higher than that of the AVRL the supplier. The government has social and political responsibility to provide clean potable water to urban dwellers to meet its

**Table 7.6 Summary of Results: Pre-contractual Analysis of GWCL and AVRL**

Buyer Power Resources (Indicators)	Supplier Power Resources (Indicators)	Buyer-supplier power structure
<p><u>Utility</u></p> <p>Less share of supplier's turnover. Contract value forms 1.09% of supplier's total annual turnover, limited volume to leverage the service provider,</p> <p>Transaction has substantial appeal Little information on suppliers cost base Limited volume of demand to leverage supply market but has prestige.</p>	<p>Larger share of GWCL's business needs Lower transaction value to total business turnover. Transaction has some prestige value</p>	<p><u>Supplier dominance</u></p> <p>A &lt; B = dominance</p>
<p><u>Scarcity</u></p> <p>Only AVRL reached preferred supplier status unchallenged. Time sensitive to sign the contract Supplier selection constrained by specialist nature of the service offerings Cannot substitute or redesign the water contract Few suppliers keen to take on management services Limited barriers to entry due to specialist nature of services Significant dedicated assets and high switching costs.</p> <p>Time constraints. GT keen to sign the contract as quickly as possible</p>	<p>Lack of active interest from foreign companies to compete for the contract.</p> <p>Wide business network and options available to develop business opportunities</p> <p>Entry of alternative suppliers but restricted by perceived political risk in the delivery of telecom services</p> <p>Other business opportunities available</p>	<p>A &lt; B = supplier dominance</p> <p>A &lt; B = supplier dominance.</p>
<p><u>Information</u></p> <p>Limited information on supplier's costs and returns. Limited information on supplier's management systems and performance</p>	<p>Full access to GWCL's expectation from the contract ie Ghanaian newspapers, websites, World Bank websites, historical experience, Ghanaian government officials. Industry practice and benchmarks.</p>	<p>Overall AVRL is dominant</p>

Key: A= Buyer Dominance  
B= Supplier Dominance  
C= independence  
D= Interdependence



Commitment under Millennium Development Goals (MDGs) of the UN by the year 2020 (Ainuson, 2007) and also to meet its electoral promises.

By contrast, Table 7.7 and Table 7.8 show that the service provider's relative utility in the water transaction appears to be low.

**Table 7.7 Summary of Results of GWCL Interviews**

Buyer (GWCL)	Suppliers (AVRL)
<p>Utility</p> <p>Operational: The contract with AVRL is critical to the continued operations of the water company:</p> <p>Government obligation to provide water services to 80 communities.</p> <p>Government's is signatory to the MDGs to make water accessible to everybody.</p> <p>Water services linked to health and sanitation needs of the people.</p> <p>Importance: Critical to the government's performance in political office ie meeting MDGs of safe drinking water for all by 2015</p> <p>Alternative suppliers: Three companies: Suar of Paris, BiWater UK, and AVRL of Netherlands indicated interests but only AVRL remained as the preferred buyer</p> <p>AVRL as the only supplier at the supplier preferred stage.</p> <p>Water market structural barriers: Few specialised suppliers in the market</p> <p>Non-substitutability: No feasible alternatives to water provision or alternatives</p> <p>Time sensitive: reliant on the AVRL for the project to take off</p> <p>Information:</p> <p>The negotiation team had a good idea of what they expect from the contract but had no information about supplier's lowest acceptable price.</p> <p>GWCL was not privy to AVRL's cost schedules and mark ups</p>	<p>Utility high Transactional salience</p> <p>Supplier scarcity</p> <p>Information asymmetry</p>

One of the main issues a typical supplier might consider is whether a buyer's transaction is valuable to its operational or commercial needs, i.e. the relative size of the GT's expenditure relative to the volume of their business (Lonsdale, 2005a; Cox et al, 2001).

**Table 7.8 Summary of Results of AVRL Interviews**

Supplier AVRL	
<p>Operationally:</p> <p>Ghana's water transaction not considered as core to their operational performance.</p> <p>Contract serving as a stepping stone for AVRL to enter the African sub-region</p> <p>Commercially: water contract value ratio to total Turnover is 1.09%.</p> <p>Buyer Scarcity</p> <p>AVRL had other markets to take their business; is a part of Norwegian Telecommunications group with extensive operations in 18 countries in Europe, South East Asia and North America.</p> <p>Information</p> <p>Had a team of experts and project risk assessment team</p> <p>AVRL had considerable experience in the past of project pricing</p> <p>Possessed private information on prices and cost of the contract.</p> <p>GWCL shared project information including indications of how much GT was prepared to pay for private sector managing the facility.</p> <p>Supplier was aware how much international funding was available for the project</p>	<p>Moderate transactional salience to</p> <p>Low buyer scarcity</p> <p>High information</p>

Documentary evidence from the company's websites shows that the turnover of the turnover of the Dutch company, Vitens-Evides, at the time the contract was signed was \$700million, whilst that of Rand Water South Africa, the other company in the consortium was \$400million (Vitens- Evides, 2010) totalling \$1.1 billion.

On other hand, the contract value of the urban water is \$12 million represents 1.09% (0.017 or 017% for Viten-Evides and 0.03% for Rand Water. Given the low value of the water contract relative to the service provider's business turnover, it is reasonable to conclude that the GWCL contract, although has prestige value, in terms of attractiveness, is of low utility. In that sense the government may have limited opportunities to leverage the supplier. Another area that the supplier may consider is whether there is any possibility of future business after the end of the contract. If a typical supplier finds that a contract could be renewed then the supplier will consider it strategic to its future profitability prospects and may be motivated to work collaboratively for future business. In that case the supplier is in a favourable power position to leverage the supplier for cost improvement (Cox et al, 2001). However, in the water contract case, uncertainty remains- whether it would be fully privatised or the contract will not be renewed by a new government. This uncertainty will not increase the bargaining leverage of AVRL.

In terms of supplier availability, results displayed in Table 7.8 show that GWCL faced supplier scarcity. At the close of the tender, AVRL remained the only supplier up to the preferred supplier stage. The explanation given is that out of the three companies who responded to the advertised contract only AVRL remained as the only interested company up to the preferred stage. The other possible reason is that two suppliers who withdrew their bids may have considered the water contract unattractive enough to warrant their diversion of resources elsewhere to develop the relationship. Another reason could be that they found the contract too risky to manage. Thus the government is confronted with the problem of creating supplier choices to improve his options.

By contrast, the supplier appears to have options in the market. The profile of the consortia behind AVRL, Vitens-Evides International Company shows that it is engaged in extensive business activities in Mongolia, Vietnam, Yemen, Malawi and Surinam in water management systems while Rand Water South Africa is working in Mozambique as well as in South Africa. It is possible to assume that AVRL or the consortia can develop its business in other markets. In this sense, the service provider may be indifferent as to whether they win the water contract or not. Additionally, the position of AVRL as the only interested company available to the government, at least, in the short run strengthens the bargaining position of the service provider.

Moreover, it is also possible for AVRL to substitute the water contract with another one easily and the actual loss of it would only constitute as opportunity cost to the company. From this supplier's perspective, loss of the contract is not likely to affect the business fortunes of the company. This gives AVRL more leverage over the Ghanaian government.

Turning to the low supplier interest in the water contract there may be several reasons to account for that. The major ones are that most foreign investors consider water industry as risky investments because of uncertainty over government control over water services and policies on tariffs especially in developing country like Ghana (Ainuson, 2009). As a result, only few suppliers are likely to invest or work with Ghana government albeit on their own terms. The other reason given at the interview is that the water industry has some technical and financial entry barriers for many suppliers given the specialised nature of the operations. In view of that the few suppliers who exist choose which country to work based on the level of value capture and at low risk acceptance.

We also note that the government faced time constraints to conclude the contract with the only available supplier to pave way for early commencement of the water project. The other option is to wait until it has been able to stimulate competitive interest among prospective suppliers. The problem for the government is that over four years have been spent in search for a qualified and willing partner without success and now faced national water crises with an urgency to conclude the contract as quickly as possible. Further delay in signing the contract with AVRL will also mean undue delay in project completion time. Moreover, the government is going into an election in two years' time and water provision is a critical key electoral triumph card in a country like Ghana. Furthermore, any further delay in signing the project also means that the government cannot access the World Bank loan for the urban water project until a partnership is formed. Based on these considerations, the government may be prepared to sign the contract with less than ideal terms rather than incur delay and searching costs and possibly lose the impending elections to its political opponents.

On the supplier side, it appears that AVRL is not constrained by time to sign the contract, therefore has the incentive to sit out on the contract until all its terms are met. In other words the difficulty of arranging or getting an alternative supplier in place on short notice introduces some form of hold-ups and loss of bargaining power (Masten, et al., 1991, p.9). Given the above analysis the supplier has opportunities to leverage the government for enhanced deals.

The last key power resource is information. Results also shows that the service provider was better informed about the GWCL's budget for the water contract. While TMP obtained information from the World Bank website and also from the tender documents, GT officials may not be aware of the lowest price the service provider is prepared to accept. There is no

indication from the interviewees that AVRL shared their cost structures with the government. Given that AVRL as a profit making entity wants to maximise its profits, it has incentive to price its services at the maximum price obtainable in the industry. Meanwhile, information asymmetry on the part of the government may make it difficult for AVRL cost projections to be verified as to its fairness or reasonableness. From this perspective, AVRL has bargaining leverage over the government. These factors are summarised in Table 7.6

In putting all the variables together we can reasonably reach the conclusion that the service provider has more favourable pre-contractual power than the GWCL and it fits squarely into the dominant partner framework. Also going by the standard power-dependency theories (Emerson, 1962, Pfeffer, 1978; Cox et al., 2001) mean that AVRL will have more bargaining power and be able to dictate the terms of the contract.

#### **7.6.1 Analysis of Factors Resource and Negotiation Capabilities**

This section uses the evidence gathered at the interviews to evaluate the potential existence of asymmetry in resources and capabilities in negotiations between GWCL and AVRL. The primary hypothesis predicted that asymmetry in resources and capabilities will impact on the ability of public sector manager to design a balanced contract. Data used in the analysis is mainly from the interviews. To establish that an asymmetry exist between the GWCL and AVRL, key indicators used were negotiators experience, commercial knowledge and technical competence and independence in taking the contract decisions were obtained and

compared. Using the metrics we designed in Chapter 5 results showed that there was indeed asymmetry between the GWCL negotiation team and the AVRL representatives

### **7.6.2 The Negotiation Resources and Capabilities of GWCL and AVRL**

This section analyses the relative abilities of GWCL to communicate and negotiate with the service provider on equal terms. One of the key factors in successfully managing a partnership relationship is the ability of the client's negotiation team to competently and professionally engage the private sector in negotiations at equal strength so as to design a balanced contract. This means that the procurement department or the negotiation team should be adequately resourced in terms of negotiation skills, knowledge and experience and ability to plan and execute negotiation strategies for best deals..

The importance of a well-resourced, capable negotiation team to the design of a balance contract terms was well understood by GWCL staff. However, the study identified that, as in the telecoms case, less attention was paid to presenting a well-resourced and capable negotiation team for the water contract negotiations. All the interviewees from GWCL, including the DCEO and GOF1, were unanimous that the government negotiation team performed poorly against the service provider, because the team was ill-prepared for the negotiations. Specific mentions were also made about the government's lead role in the selection and award of the contract to AVRL. The GOF1 conceded that it is established practice for the government of the day to contract on behalf of public sector bodies, especially when foreign contracts and agreements are involved. He provided two reasons for

the rationale behind the government's intervention in the water contract and in other high profile contracts with TNCs. First, he intimidated that the ultimate responsibility for the payment or liability for any default on the water contract lies with the government. Second, the international community only negotiates with the government and not a public sector body. GOF2 conceded, however, that the direct involvement of the government in the selection and award may have compromised the integrity of the negotiation process.

Although the interview could not obtain the specific professional qualifications and experience of the negotiation team, it is easy to infer from the responses from interviewees that the service provider negotiation team was more resourced than the government-led team that represented GWCL. When asked about the quality of the team, GOF2's response was that:

‘Members of the negotiation team were selected from the Finance Ministry, the Attorney General's department, a representative from GWCL and government officials...and looking at the selection my view is that members have no background or experience in contract negotiations.’

GOF2's assessment was that the government team was ill-prepared for the challenge and may have affected their sense of judgement on contract signing. He admitted that:

‘A lot of mistakes were made during the negotiation, simply because the team we sent to the negotiation table was ignorant about what a contract negotiation was all about and failed to plan for it.’

PMU2 further admitted that the contract language was too technical and except the representative from the Attorney-General's Department who seemed to have a better understanding the rest of the team did not understand what they approved.



In contrast, the interview with the supply side showed a different picture, of a well prepared negotiation team. The background of the AVRL team was described as professional by HRM2:

‘We presented a strong negotiating team who understood the market needs of the water industry in general that of GWCL, our own needs and developed an approach relevant to our expectations from the contract negotiations’.

Although he declined to give specific details of their educational backgrounds, it was clear that each member of the team came with unique experience, knowledge and skills. Without directly mentioning any specific qualifications, CEOW described the competency of members of the negotiation team as highly trained. According to the CEOW they approached the water contract pre-contractual negotiations with the right people with clear strategy to bring the best results. Touching on the quality and competency of the negotiation team, he stressed the point that

‘We relied extensively on our experience acquired in past negotiations...we picked our team carefully. Every member of the negotiation team possessed both professional qualification and experience and our confidence is high believing that they know what to do to get us the best possible.’

Overall, the general perception from the interviewees from the public side (GWCL management and government) when questioned on knowledge, skills and education, admitted that the AVRL team were superior to that presented by the government

Results in Table 7.9 and 7.10 show the composition of the both GWCL and AVRL negotiation teams. From the table, a representative from GWCL (technical side) Ministry of Finance served as a witness and a representative from the Attorney General’s department.

From this composition, it is evident that none of the GWCL team has any strong procurement background.

**Table 7.9 Summary of Negotiation Resources and Capabilities in Negotiations of GWCL and AVRL**

Resource and Capability :	GWCL	AVRL
Composition	A representative each from the Ministry of Finance and Economic Planning and Attorney General Dept. Technical Director of GWCL and a representative from the government.	Sales and marketing department Negotiation team drawn from the two parent companies' Sales and marketing departments
Experience	None of the members had any previous engagement in similar transaction	Negotiation team has engaged in similar contract negotiation elsewhere
Commercial knowledge/Skills	Exhibited low commercial and understanding of the transaction. Did not conduct project economic analysis	Two members trained in contract negotiation and analytical skills. Capable of understanding and analysing the technical and financial, requirements of the project.
Independence	Team was prevailed upon to accept the contract terms and sacrificing professional judgement	Applied independent and professional judgement in line with organisation's objective of maximising profits.
Deployment of	Barely responded to supplier's contract proposals	Able to push their proposals through and overrides the GWCL's team strategies

By contrast, the AVRL negotiation team are all from the sales department and led by the head of the negotiation unit. The composition has the precise mix of negotiation attributes to achieve good negotiation results. There are two possible indications that either supports the conclusion about the superiority of the AVRL negotiation team. Firstly, the contract document was drafted by the service provider and presented to the GWCL side (PMU1). Secondly, the negotiation team did not subject the contract document to strict scrutiny. From the public sector side, GWCL's side, the reason for approving the contract document presented by the AVRL was that the government was in haste to sign the document.

**Table 7.10 Mapping of Negotiation Attributes of GWCL and AVRIL**

	GWCL	AVRL	Symmetry/asymmetry
Previous experience	No evidence of previous engagement or familiarity with commercial negotiation	negotiations in previous transactions elsewhere	Asymmetry
Skills: Commercial/knowledge	Low degree of training. PMU given two week crash course	Formal training in procurement and in contract negotiations	Asymmetry
Independence	Negotiation team appointed and directed by the government throughout the bargaining process	Worked independently as professionals	asymmetry
Deployment	Unable to challenge AVRIL proposals : failure to conduct hard bargaining	Responded strongly to GWCL strategies	Stronger for AVRIL
Technical knowledge of the project	Knew the project requirements but less knowledge in cost-benefits analysis	Used their technical staff and project/ investment appraisal staff	symmetry

Another perspective obtained during the interviews was that the GWCL negotiation was ill-prepared in terms of negotiation strategy. Given the background of the members AVRIL negotiation team past experience it is reasonable to expect their project appraisal team to gain upper hand with weakly-resourced and ill-prepared AVRIL negotiation team.

The incompetency of the GWCL negotiation team is made clearer when some of the members found the legal language hard to comprehend and to understand. Based on the analysis that GWCL negotiation team lacked basis knowledge in negotiation skills and experience, we can reasonably assume many possibilities of the government team signing a contract containing traps to hold-up the government in the contract. However, we find the link between asymmetry in resources in negotiation and capabilities to contractual lock-in for the Ghanaian government to be weak but significant enough to deepen the already adverse pre-contractual power relation.

## **7.7 Conclusion:**

In summary, the analysis showed that the AVRL has a favourable bargaining power in the relationship with the government. Firstly, the utility in the supplier's offerings is found to be higher than the commercial attractiveness of water transaction to AVRL. Secondly, as a result of time constraints and lack of equal qualified suppliers in the industry, AVRL is considered as an important scarce resource that must be acquired. Finally, while AVRL is better informed about the critical information about cost and returns the public sector side had limited information about the suppliers cost and margins, therefore was unable to challenge the supplier's price proposals. In combination, and going by the resource and dependency (Emerson, 1962, Salancik, and Pfeffer, 1977; Cox et al., 2002, 20020. We can reasonably conclude that GWCL was in an adverse pre-contractual power position which to GWCL means it is in a weak pre-contractual bargaining position to leverage AVRL.

Despite the above analysis, it is important also to observe that suppliers may not fully disclose their high utility in a particular transaction for commercial reasons, to the buyer. This question came up during the interview and the CEOW was hesitant to make definite stand on relative importance. It is therefore important to observe that our restrictive analysis suggests that the telecoms contract is relatively important to the GWCL; there is possibility that AVRL utility is equally high but this was not adequately exploited by the government.

## **7.7 Post –Contractual Balance: the Evidence**

The main aim of this section is to analyse from the empirical data to establish whether there is evidence of post-contractual balance between GWCL and AVRL. The first hypothesis is

that there will be post-contractual imbalance arising from the adverse pre-contractual power relations. Consistent with the proxies in our methodology chapter for the measurement of post-contractual balance, our analysis focuses on whether:

- i) The terms and conditions of the contract exhibit a fair representation of what each party in the relation expects and do not impose onerous obligations on one party and not the other.
- ii) Underlying specific assets were equitably shared, or in the absence of that, financial hostages were posted.
- iii) The contract design integrates the necessary incentive structures and self-enforcement agreements with necessary incentive structures, i.e. postings of ‘financial bonds’ to sustain mutual inter-dependent relations post-contractually.
- iv) There was open sharing of information and transparency (open book system).

The analysis is based on the results of study obtained from the interviews and other documentary sources.

### **7.7.1 Relevance of Risk and Uncertainty in the Water Supply Sector and Management**

We examine the presence of contractual balance in the water contract through the analysis of whether risk and uncertainty are equitably shared. The objective of the empirical analysis presented here is to study whether adverse pre-contractual power relation of the GWCL created post-contractual imbalance. In a typical standard TCE theory, dictates the public sector should share or allocate risk and uncertainty to the private sector to balance risk so that

both parties face similar high switching costs. A contract designed in this form will create mutual dependency relation and reduce opportunism (Williamson, 1983; Blankenburg et al, 1999). The relevance for risk sharing and allocation is important given the level of uncertainty in the water supply operations in Ghana.

The water company is a service industry characterised by political, social and economic factors and may have some inherent uncontrollable elements. Thus its operational outcomes may be affected by considerable risk at both the operational and commercial level for both the contracting party and the agent. For a contracting party to maximise its returns, it must understand the dynamics of the market and the commercial outcomes. This takes into consideration revenues and cost and factors that influence them whether controllable or otherwise. In the water sector, income depends on water sales, but this in turn, depends on water sales and tariffs policy (Gilbert, 2007; Lewis and Miller 1987).

The characteristics of Ghana's water system do not differ significantly from most of the developing countries. In common with most water companies, elsewhere, the water supply system is shaped by government policies and unpredictable political games and electioneering campaigns. Another uncertainty facing the water industry is financial losses arising from theft, illegal connections, and defaulters. These are difficult to control and in case of defaulters, it is difficult to arrest for prosecution as a result of government's lack of political will.

Significant problems also exist in the water supply management owing to centralisation policies. Studies in developing countries suggest that most water companies run at a loss because the government does not allow cost recovery charges to prevail in order to protect the lowest income earners (Lewis and Miller, 1987). Although GWCL's business objective may be full cost recovery, political pressures have determined the actual tariff set low to make water affordable to all but to the investor is a loss to business operations (Katharina, 2001).

Furthermore, and related to above is uncertainty in water revenues. In most developing countries like Ghana, the government often intervenes in water tariff setting to make water affordable to people who live on US\$2 a day and may not afford to meet full cost recovery pricing (Director-General Dept., 2010). From this perspective three issues can be identified in terms of revenues and costs in GWCL's operations. First, it is difficult to determine monthly revenues in advance, because that depends on how much water is demanded and paid. Secondly, In the case of cost, monthly expenditures are not fixed, because the cost of supplies, repairs and maintenance fluctuates depending on requirements. Thirdly, the government can nationalise foreign water companies (Lewis and Miller 1987). All of these factors have made it difficult to keep operating costs down or revenues up and therefore the industry is characterised by considerable risk and uncertainty. From the private investor perspective, such a venture is too risky. In those circumstances, a risk adverse investor would avoid taking up risk in the company where revenues cannot be guaranteed and cost fluctuation is the norm.

On the buyer side, there is a need for the government to manage the relationship to achieve its strategic goals, but that depends on the activities of the private sector partner. The

government is faced with uncertainty because the level of effort required to perform the service in a way that satisfies its strategic objective of getting value for money is not known.

The option opened to the buyer side is to use risk-incentive trade-offs to control the behaviour of the agent in a way that promotes its interests. Whether the government can achieve this depends on the amount of leverage it has in the relationship. Unfortunately, it seems that the government in this specific case has not got the sufficient amount of leverage to design efficient risk-incentive contract to allocate part of the risk to AVRL. There are many issues in the contract suggesting that risk and uncertainty were not equally shared in the relation with particular reference to fixed assets investments and contract pricing plan. Besides that the government faced high switching cost, contract rigidity and information asymmetry. We look at each in turns.

### **7.7.2 Risk Sharing: Fixed Assets**

The water contract would have to be supported with transaction-specific investments in the area of water treatment plants, pumping stations, and dams. TCE logic provides these transaction specific assets should be shared equitably in order for the party with more risk to avoid becoming locked in by the party with less risk (Williamson, 1983).

Evidence gathered from the interviews showed that the Ghana government, represented by GWCL was solely responsible for infrastructure development. We found no indication that AVRL made physical investment in the water company infrastructure. This means that GWCL took all the investment risk. This could be interpreted to mean that the government could not get AVRL to agree on the question of investing in the company. It also appears that



the government is dire need for external intervention in managing the water service delivery but in the absence of alternative suppliers may have to persuade AVRL to agree to the formation of the partnership. As a result, GWCL had to agree to accept the risk in the relation.

The decision of the supplier not to invest in the dedicated assets in GWCL can be explained by suggesting that a supplier will not invest in dedicated assets in a relation if the company has low volume requirements or the company offers few opportunities to develop further business. Either of the two appears to be absent in the water contract. Even though, the water project may be subject to a renewal at the end of the contract in 2011, uncertainty remains over whether the contract will be renewed or sold outright. This shows that the AVRL would use its pre-contractual power to avoid taking risk in the relation.

### **7.7.3 Risk Sharing;; Contract Cost and Incentive**

Findings show that the contract pricing plan chosen by AVRL was a fixed contract sum. This means that AVRL received a guaranteed income from GWCL operations irrespective of performance. The implication is that AVRL strategically avoided taking risk and uncertainty thus shifting the relationship balance to its favour.

As it happened in the first case, the service provider further retained an exclusive power to collect revenues and make disbursements at its discretion. In this way AVRL is able to minimise its own risk and uncertainty as a precaution against losing out in net contributions if

it turns out that future revenues are higher than what was anticipated had variable contract was chosen. The terms of the contract under Section 6.3.2 provide that:

“The Grantor hereby irrevocably grants to the Operator for the Management Contract Period the care and control of the Revenue Collection Account, which shall be operated exclusively by the Operator pursuant to the terms of this Management Contract. Subject to the availability of the amounts, the Operator shall pay from the Revenue Collection Account operating expenses” (GWCL and AVRL Contract, 2006).

Under the terms of the contract AVRL opened a separate account and all monthly takings from water sales were lodged in that account. From the account, all the administrative and operational expenses were paid from and balance, if any, is transferred into GWCL main account. This shows that the supplier had complete control of the GWCL. This arrangement is significant because it clearly demonstrates the power position of AVRL in the relation.

#### **7.7.4 Information Asymmetry**

The next indicator of the service provider’s influence is information asymmetry. In any genuine and balanced partnership, partners freely share and exchange key information pertaining to critical areas in the relationship. One major concern among the interviewees in terms of information access and sharing is that AVRL did not share key information with them and reporting procedures were not always followed (DCEOW). AVRL reports are routinely released late and access to the books is restricted. In addition, AVRL ultimately did not observe principles of transparency and open book systems with GWCL as genuine partners do, clearly demonstrating that the collaboration was adversarial (Cox et al., 2003). Suppliers can succeed in turning a collaborative relationship adversarial when they are dominant.

### **7.7.5 Sovereign Guarantee and High Switching Cost**

Similar to the telecoms contract, the service provider forced the government to post two financial instruments, one in the form of government sovereign guarantee and the other in the form of political risk insurance cover to the benefit of the service provider. The effect is that the government is pushed deeper into a virtual dependency position in the relation. In such circumstances, the government has got an option to demand an appropriate financial bond from the service provider to create a balance. However, the failure of government to compel the service provider to do so provides further indication that the government may be in adverse post-contractual balance with the supplier.

### **7.7.6 Contract Rigidity and Contract Renegotiation**

A final indication to suggest that the relationship is imbalance can be identified by how the contract terms are crafted to protect one of the party's interests in the relation.

During the implementation period, the government probably realised that there is high information asymmetry in the running of the company's account. A subsequent attempt to seek a revision in the a clause that empowers the service provider to exclusively manage the GWCL's revenue accounts and disbursements with the aim of introducing transparency in the handling of the company's revenues and costs failed primarily because AVRL threatened to withdraw from the relationship. An appreciation from the demand side seems that the government considered the services rendered by AVRL to be essential and was not interested in creating tension and misunderstanding that may lead to contract termination (GOF1). The weakness of the government relative to the service provider demonstrates clearly that the

government was heavily dependent on the supplier; hence power asymmetry can be seen in the relationship.

In summary, the combination of risk not shared equally, information asymmetry, contract rigidity sovereign guarantees and switching cost one can reach the conclusion that the relationship is not balanced. In effect, the relationship between GWCL and AVRL can be classified as adversarial in favour of the service provider.

Having first established that the post-contractual balance is in favour of AVRL, we proceed to examine whether this was caused by the adverse pre-contractual power relations. The first hypothesis is that the adverse pre-contractual position of the public sector organisation will make it difficult for it to develop post-contractual balance. In performing the analysis, we could examine the agreement itself, which can be a good starting point to know whether the contract is balanced or not but this will not serve any useful purpose since this has just been done. We need to look at power positioning of the two parties prior to the contract negotiation. In doing so, we are interested in who had the power at the pre-contractual contract stage to leverage the relation in his favour. In other words, the dominant party will most often force the weaker party to take more risks at the contract design stage.

This takes us to the theory that the party who that enjoys favourable pre-contractual bargaining power dictates the terms of contract. The results from our earlier analysis on pre-contractual power relations in Chapter 7.6 showed that AVRL enjoyed favourable pre-contractual power. Supplier's power is derived from the importance of the AVRL services to the operational importance of GWCL. The supplier is enjoying its status as irreplaceable, at least in the short run, couple with high switching costs. Both tend to create power advantage

for the service provider. The implication is that AVRL had sufficient pre-contractual bargaining power to dictate the terms under which it is prepared to collaborate with GWCL in the transaction. The success application of service provider's dominance to its advantage is amply demonstrated in its ability to force the government to take more risks and uncertainty, while it retained little or no risk. Additionally, the service provider may have exploited its power advantage to overcome any resistance from the government, and more crucially, the ability to determine how much of the stream of revenues coming from the collaboration go into GWCL's account.

From the buyer's perspective, it could reasonably be inferred that the government was compelled by its weak pre-contractual bargaining position to accept the terms of AVRL in order to get the service provider to agree to collaborate. On this consideration, the government may be prepared to accept to take all the risk and uncertainty upfront hence failed to achieve a balance in the relationship.

In the context of designing the contract to craft extra-safeguards to protect itself from post-contractual hold-up and opportunism in the manner suggested by TCE ,the government failed principally because the government was heavily dependent on the service provider and has not sufficient opportunities to force the service provider to take significant portion of the risk. Even if the government enjoyed favourable pre-contractual power relations, the government credible commitment given earlier, put the government in a disadvantageous position to create a balance.

Given the above analysis, we can reasonably conclude that the adverse pre-contractual power relationship contributed significantly to the adverse post-contractual balance of GWCL's relationship with AVRL.

Having coming to this conclusion, it is important to observe that other factors may be present apart from the variables analysed in this study that can contribute to post-contractual imbalance between a buyer and a supplier. Therefore it is difficult to conclude that any contractual imbalance that has occurred can be exclusively attributed to the adverse pre-contractual bargaining power. By the same reasoning, if a buyer is in an adverse pre-contractual position, it does not necessarily mean that a hold-up has occurred or the buyer is in an adversarial relationship. For this reason we examine whether the adverse post-contractual balance of GWCL had any impact on supplier performance.

To conclude, the chapter presented the interview data and proceeded to analyse the power structure and found that the government's pre-contractual balance was adverse. Evidence from the study, suggests that the pre-contractual power relationship contributed significantly to the post-contractual imbalance for GWCL. Based on the evidence analysed, the first hypothesis is supported. In the next section, we examine whether the adverse post-contractual balance of the Ghanaian public had an impact on the level of supplier performance as stated by the second hypothesis.

## **CHAPTER 8**

### **Dependent Variable: Supplier Performance**

#### **8.1 Introduction**

In this chapter, detailed analysis of PPP policy implemented by the Ghana government on telecoms and water service delivery is undertaken to investigate whether the post-contractual imbalance discussed in the previous chapter has a significant impact on supplier performance. The second hypothesis states that adverse post-contractual power relations would result in poor supplier performance. To find out, consideration is given to the minimum performance required by the Ghanaian government in each of the two contracts from the private sector partners. The objective is to establish whether the government achieved the anticipated minimum supplier performance in functional delivery and cost savings from the collaboration, and if not, whether the poor performance can be explained by its adverse pre-contractual balance. The chapter is structured as follows. Part I examines the supplier's performance in the telecoms contract. Part 2 examines the supplier's performance in the water contract.

##### **8.1.1 Review of TMP's Performance During Contract Period**

This first part of this chapter focuses on the analysis of the supplier's performance in the telecoms contract. Consideration is given to the performance that occurred between January 2003 and December 2006 when the contract came to an end. Evaluation of supplier performance in the telecom contract is based on data obtained from the interviews with GT

and TMP executives, public officials documentary evidence including and company files, and audit reports. The analysis indicates that the Ghanaian government failed to obtain good supplier performance and that this was caused by the adverse pre-contractual balance in the relationship.

During the tenure of TMP, significant successes were recorded. Analysis shows that there was an increase in the number of telephone lines fixed and internet connectivity. Before the introduction of the private sector management, fixed telephone lines for rural coverage lagged behind the urban centres. Telephone lines concentrated in the urban areas was about 55% in the Accra region, although the population in the region houses is only about 25% of the country's population (Frimpong, 2007; Osiakwan, 2007). On taking over the management of the company, TMP executives increased telephone lines in rural communities by 15%, to close the urban digital divide. In the case of internet users, this increased from a level of 0.15 per 100 people in 2000 to 1.81 in 2006 (see NCA, 2006; Frimpong, 2007). With regards to ICT in schools, TMP executives made new internet connections to 251 educational institutions. Prior to the contract most secondary schools did not have access to internet and the few computers available were mostly used in administrative work.

Prior to the PPP policy in telecom management, one of the problems identified as creating a drain on the resources of GT finances was over-staffing and inefficiencies. Staff response times were found to be poor and slow to respond to consumer complaints or attend promptly to fault reports. In taking over the management of GT, TMP executives was able to reduce the administrative staff numbers and introduced labour productivity and bonus schemes to motivate the staff. In addition to this, technical staff received further training, both locally



and abroad, to upgrade their technical skills through training schemes. As a result, staff efficiency and response time increased and the wage bill reduced.

The above performance suggests that TMP executives made a positive contribution to the overall governmental socio-economic objectives and the expectations of the sponsors of PPP. However, to examine whether this performance clearly represents the minimum performance required by GT, we need to compare this performance against the pre-contractual level of performance. To examine this, we consider Table 8.1 which presents the expected and actual performance. By comparing the expected fixed telephone installations, mobile phones and ICT with actual numbers installed or provided, it appears that TMP failed to achieve its minimum targets required by the government although the performance in the fixed telephone lines was close to target.

**Table 8.1 Key Performance Benchmarks and Achievement**

Particulars	Target Set to be achieved by 2011	Observed Outcomes	Shortfall
Fixed telephone lines	400,000	41,857	10%
Mobile phones	750,000	412,618	55%
Secondary School Internet Connectivity	485	251	52%

Source: Frempong 2007

The table shows that the TMP management team was able to install only 41,857 fixed telephone lines out of 400,000, representing just 10% of the number that the service provider was supposed to provide. In the mobile phone sector, TMP achieved only 45% of the expected mobile subscriber base while 48% was achieved in ICT provision to schools and

colleges. It is evident that although TMP performed more creditably in the expansion of fixed telephone lines, than the mobile and ICT targets, overall the performance fell below the minimum expected performance.

The other performance area with which the GT executives interviewed expressed dissatisfaction was service quality. Service quality remained poor in areas of voice quality, dropped calls, and slow internet services (Frimpong, 2007; DCEO2). There were frequent weak signals with some communities not covered with telephone or internet services.

The explanation given was more to do with technical than administrative matters. The Ghanaian government usually sources funds from the donor community. Often donor countries require the funding should be used to purchase equipment from their countries. As a result, GT have in operation switches from six different manufactures, contributing not only to poor quality service but also to high maintenance and repair costs (Osiakwan, 2007). The technical director of GT also pointed out that the problems with the inter-connectivity of international calls remained because of the complexities associated with telecoms transactions.

An appreciation of the problem from the supplier's side is that the performance of the private service provider may have been affected by the Ghanaian government's lack of resources to provide the required investment funds to carry out the planned rehabilitation and expansion programme. During the course of the interview with TMP executives (OP2; DOO2), it was explained that their efforts to extend telephone lines and internet services to the areas specified in the contract were stymied by inadequate infrastructure funding on the part of the government. In relation to poor quality service, TMP executives explained that the existing

systems and equipment were obsolete, therefore unreliable, affecting their operations. Although this was brought to the notice of the government and they received assurance that the old equipment would be replaced with modern cutting-edge technology, nothing was done about it. However, the service provider's version of the problem is challenged by evidence of government's secured funding and invested almost US\$500million into equipment rehabilitation and new purchase (DOO2; PO2; Frimpong; 2007).

### **8.1.2 Financial Performance**

The second key criterion which TMP management was required to achieve is making GT financially stable by adopting waste reduction strategies including staff fraud as well as exploring new business activities that increase value to the company and at the same time adopt waste reduction strategies include staff fraud. Although no specific target was stated for TMP to achieve, the government expected TMP to adopt cost effective process in its activities, and continuously exploring value adding processes that will save cost.

This objective in cost savings is important to Ghana in the transaction. Before the introduction of the private sector initiative in the management of GT, the government and the World Bank officials were concerned about GT's high operating costs, although the project consultant saw many areas which, if exploited, could have brought about more revenues and profits. As a result, the government's expectation was that these cost savings opportunities would be exploited fully by the incoming private management services team for the benefit of the public sector.

Under the old management, GT was annually turning up losses. Between 1999 and 2000, GT operations recorded a drop in revenue from US\$170 million to US\$89 million (Osiakwan, 2007). Among the major causes were poor financial mismanagement, political interference, low tariffs, fraudulent practices and the impact of global developments on GT operations. However, this changed when TMP took over, at least, in the first year of operations.

Although, there is no reliable data on operational and administrative costs because official data could not be obtained, this can be estimated from the company books, audit reports and other published data about the company's affairs. Between 2003 and 2004, profit increased from a loss of \$21 million in 2003 to \$12 million, representing an increase of \$33 million. This shows a remarkable achievement given that prior to the TMP contract GT was recording losses (Ghana Audit Service, 2001-2003). However, it appears to the government that this expectation of sustained high profit levels was not entirely fulfilled. For example, profit started to reduce after the first year success.

The data shows that despite the initial high financial performance, turning a financial loss of US\$21 million standing in the GT books before the takeover to a profit of US\$12 million (i.e. a profit of US\$33 million) during the first year, profit started to decline significantly between 2004 and 2005. Table 8.2 shows that GT's profits fell from US\$33 million in 2003 to US\$11 million in 2004 and rose slightly to US\$17 million in 2005. The downward trend in profits suggests that GT began to receive a sub-optimal performance from TMP.

Furthermore, in the absence of detailed internal data to assist in determining the actual revenues that should have been accrued, the study decided to compare the financial

performance of GT to another close competitor, ‘Areeba’ in the mobile telephony market using published data about the company’s affairs.

In Table 8.2 comparing GT revenues with ‘Areeba’ telephonic company, data obtained and compiled from newspapers and other reports (Public Agenda, 2006) it is noted that while GT’s profits were rising by small amounts, Areeba’s activities saw significant annual jumps in profit over the same period from \$181.2 to \$355 in 2005, between 150% and 200%. From this simple comparison between TMP and Areeba, not accounting for internal competencies and commercial drivers, it appears that TMP has not been effective in controlling costs. The comparison of financial performance with ‘Areeba’ is significant given that GT at the time controlled 90% of the telecoms market in Ghana (Frimpong, 2007; Osiakwan, 2007).

**Table 8.2 Comparison of TMP and Areeba Financial Performance**

Company	2002 \$’m	2003 \$’m	2004 \$’m	2005 \$’m
<sup>5</sup> Ghana Telecom	(21.0)	12.0	11.6	17.5
Areeba	27	181.2	323	355

Source:Constructed from newspaper reports and company files

Interestingly, TMP executives believed that they had been working hard to achieve the objective of cost savings (DOO2; OP2; ID2). The executives argued that they faced considerable technical difficulties in expanding operations as a result of frequent equipment failure, high maintenance costs and low tariffs. They, however, attributed the problem to the

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<sup>5</sup> Unaudited accounts of GT

incompatible infrastructure purchased from different manufacturers that gave rise to frequent system breakdowns costly repairs and high maintenance.

From the above analysis however, it is evident that TMP executives failed to fully deliver on their pre-contractual promises. In addition, the evidence suggests that operational costs continued to rise disproportionate with revenues increasing the probability of not making savings. Yet the government was not able to apply sanctions or change the prevailing incentive system to force TMP executives to improve their performance. Additionally, the government could not compel TMP to operate transparency and open book policy in running GT accounts. Also the service provider decides what information and the content to be shared with GT and got away with it. Any of this supplier practice and behaviour is likely to occur when a particular supplier is dominant and the government does not have sufficient power resources to enforce contractual performance or to compel the service providers to pass over cost savings. The above analysis of government's failure to get good supplier performance warrants further careful examination, since it supports a case of supplier dominance and a possible hold-up. We will analyse this possibility in the next section.

## **8.2 Discussion**

As we noted in our earlier discussions, the telecoms operation is affected by uncertainty regarding revenues and cost. In telecoms business operations, the management relies on the subscriber base to generate the bulk of revenues and there is high level of uncertainty in revenue maximisation. This is because it is difficult to predict the number of people who will subscribe to the GT network given that there are five other competitors in the market

(Osiakwan, 2007). Even if it is possible to accurately predict the number of subscribers, it is not clear how much each subscriber will purchase.

Given the high levels of information asymmetry regarding TMP's operations in handling the financial transactions in GT creates risk of post-contractual moral hazards and opportunism (Cox et al., 2004). Post-contractual moral hazards, refers to a situation where a supplier bids low to win a contract and during the contract locks the buyer into the relation and then take the opportunity to extract rent from the relation. In this case, post-contractual opportunism can take a new meaning of post-contractual moral hazards. The initial high performance of TMP that was recorded during the first year of the commencement of the contract, raising high expectations of government started to decline. There may be one of two possible causes. Firstly, the sharp decline in profits may indicate of sharp increase in operation costs and declining revenues. In this case, inefficient operations could easily be identified and remedial action could have been taken against declining profits. Secondly, the sharp decline in profits may suggest that some portion of the revenues was not being properly accounted for in the books or costs have been exaggerated or both and dishonestly being appropriated to increase the suppliers returns. Since, there is high information asymmetry, it is reasonable to assume that it would be difficult for the government to detect it. If the supplier is extracting more benefits from the collaboration, raises two possibilities on the government's side.

First, the government did not consider that profit is a function of costs and revenues, and that the data on cost and revenues submitted by the service provider did not consider putting a cap on expenses, or stating the minimum revenue target for any specific month. This omission on the part of government provided scope for opportunistic behaviour. Given the information

asymmetry as a result of inability to access the books, it is difficult to monitor the service provider. Given that the TMP is in business to maximise profits, it is logical to assume that TMP has an incentive to under-report revenues and over-exaggerate costs, and appropriate the same to increase its return and earning economic rent. The appropriation of economic rent from the relationship could be higher if we consider the fact that the three year contract price might have been set at the maximum market price. Literature on monopoly suggests that when there is one supplier in the market, buyers suffer from monopoly pricing providing support that GT possibly suffered from opportunistic pricing (Martimoor and Stole, 1999). TMP was the sole bidder and given that the supplier market has fordable entry barriers then we can expect TMP to have sufficient bargaining power to set its price higher than normal returns pertaining to the industry. Similar to single sourcing approach, the supplier scarcity, provides incentives for TMP to set its price at the maximum possible in the telecom industry.

The standard principal agency provides that where risk of moral hazards exists, incentive schemes that tie performance to agent's payments should be considered (Holstrom, 1979; Eisenhardt. 1989). However, in this case, the incentive structure to promote collaborative relationships appears to be ineffective to address the problem of moral hazards. On the contrary, TMP was provided with guaranteed income as per the terms of the contract. When these issues are combined, it can be assumed that TMP is appropriating a larger share of the benefits than it is entitled.

However, government action can be explained by the adverse pre-contractual power relations with GT at the pre-bargaining stage. The combination of the essential nature of the telecoms contract to the government, unavailability of alternative suppliers, threats of exit and



government's credible commitment to the relationship leads to the conclusion that TMP is dominant in the relation. Additionally, given the power of TMP's ability to force the government to take all the risk and uncertainty, and the ability to decide how to perform its side of the contract and how much of the benefit to be passed to the government and nothing is done about it, supports the conclusion that the government is weak post-contractually.

To conclude, this section has analysed the performance of TMP. While TMP has achieved some success under the contract, there is evidence to show that it failed to meet the government's minimum performance requirements. Additionally, it was observed that costs were rising and revenues falling behind other players in the field suggesting that rent is being extracted from the relation. In the light of above we can reasonably conclude that the service provider failed to deliver on its promises and that this due to the fact that it was dominant in the relation.

Having concluded that, the analysis presented here on evidence of post-contractual hold-up and rent appropriation comes with a problem. A variety of reasons may affect supplier performance that may not arise from shirking or opportunistic behaviour or other circumstances beyond the supplier's control. Similarly, if a hold-up occurred (adverse-pre-contractual balance) it does not mean that economic rent was being appropriated because there could be a variety of other reasons as discussed by some writers (Klein, 1996; Coase, 2006). Similar difficulties could be observed on the buyer's side. The GT officials found it difficult to determine whether claims of rent capture occurred, presumably because they could not access the books to review the cost base and returns margins of TMP.

However, putting all the issues in the above analysis together, it is evident that TMP failed to provide increasing functionality and lower cost of ownership to GT. Furthermore, when considered against the adversarial collaboration witnessed, we can safely reach the conclusion that the adverse pre-contractual weakness of the Ghana government contributed to it failing to obtain good supplier performance and good value for money in the telecoms contract.

### **8.3 Review of AVRL's Performance during the Contract Period**

In this second part of the chapter we examine the impact of the adverse power relationship on the performance of the supplier in delivering functionality and cost. The methodology adopted here is the same as in the telecom case. Consideration is given to the minimum pre-contractual targets AVRL negotiated with GWCL at the outset of the contract and whether the government achieved cost savings from the collaboration. The objective of the empirical analysis is to determine whether the Ghanaian government received the minimum required performance from AVRL, the service provider. This will allow us to determine whether the second hypothesis that the adverse post-contractual relationship will lead to poor performance is supported. The next task is to determine whether or not the supplier performance outcome was caused by the adverse post-contractual balance. In order to analyse these issues, consideration is given to the performance of AVRL between the contract commencement in January 2003 and December 2006. Evaluation of supplier performance in the water contract is based on data obtained from the interviews with the GWCL and AVRL executives, documentary evidence including databases and files, and independent reports from the Ghana Audit Service. The analysis showed that the Ghanaian government failed to

obtain good supplier performance and that this was caused by its adverse pre-contractual balance in the relationship.

### 8.3.1 Reduction of Unaccounted Water Losses

From the data collected and documents analysed, AVRL made some significant successes during the period they were in charge of GWCL. From Table 8.3 there were increases in water production from 210.6 million cubic meters in 2005 to 231.77 million cubic metres in 2009, increasing production by 10%. In addition AVRL made 38,000 new water connections, serving 100,000 people providing more households to clean potable water.

**Table 8.3 GWCL and AVRL Performance 2006-2009**

Item	Unit	2005	2006	2007	2008	2009	% increase/decrease
Water Production	MM <sup>2</sup>	210.6	211.7	217.9	222.6	231.77	10%
Water Sales	MM <sup>2</sup>	108.88	100.1	103.9	107.6	112.3	3%
Non-Revenue Water	%	48.3	52.8	52.3	51.7	51.5	(22%) variance
Total Revenue	GHC/M <sup>2</sup>	55.90	57.65	69.4	102.26	106.6	91%
Total Cost/m <sup>3</sup>	GHCM <sup>2</sup>	54.32	62.41	57.81	87.99	90.5	66%
Chemical Cost	GHCM <sup>2</sup>	0.023	0.03	0,03	0,03	0,04	0.017

Source GWCL 2010.

One of the major problems was the shortage of water meters. Under AVRL's administration, large quantities of meters were procured and installed, increasing the possibility of harvesting increased revenues. Billing procedures were reviewed and collection points made, with the result that bill collections and payments improved considerably. According to the Customer

Care Director of AVRL, the collection rate increased from a previous 80% to 95% (DCEO; CSM).

Another positive performance of AVRL was in the reduction in the number of administrative staff. The AVRL executives cut down staff numbers and offered training courses to those retained. As a consequence, staff inefficiencies reduced considerably and staff response times improved considerably.

From above findings it appears that the AVRL executives' performance in running the affairs of the GWCL was satisfactory. The question is whether represents the accurate representation of the minimum performance required by the government. To analyse that, consider Table 8.4 which presents expected achievements and actual performance.

**Table 8.4 Key Performance Benchmarks**

Particulars	Pre-Contractual Level	Target Set to be achieved by 2011	Observed Outcomes	Exceeded/Shortfall
Financial Stability	-\$1.3m		\$10.5m	Not achieved
Non-Revenue Losses	48%	26%	51.7%	31.7%
Cost Recovery of total cost	48.4%		66%	
Water Capacity	55%	80%	59%	20%
New Connections to households		50,000 households and 350 stand pipes	38,000	25%
Water Quality		Levels of lead and mercury high		Below average standard

By comparing the number of households expected to be connected and actual number connected, it is evident that AVRL executives did not meet their contractual promises. The

AVRL executives achieved 75% of the minimum required households to be connected by January 2011. In terms of public stand pipes, no reliable data was made available during the research, even though it was estimated that by an interviewee from the GWCL (COP1) that only 35% had been fixed as at January 2011.

In respect of reducing non-revenue losses Table 8.4 showed that AVRL failed to achieve its target. Non-revenue water losses refers to the volume of water produced that is lost in transmission, from the water production stage to the final consumers (Farley and Trow, 2003; IWA, 2003). In the water industry, water losses are considered as a normal feature, and international benchmarks set to measure efficiency is 20% (IWA, 2003). Studies in water supply management indicate that losses during transmission arise for a variety of reasons. The major causes are leakages, burst pipes and illegal connections. In Ghana similar problems are found, but the other category of loss is related to unbilled water consumers. Unbilled consumers are mainly a category of households who, through no fault of their own, have not been provided with water meters to record actual water usage, and government institutions that happen to be heavy water users but do not often meet their paying commitments (Farley and Trow, 2003; IWA, 2003).

The significant of water losses is that it has direct impact on revenues generation. The higher the percentage losses, the less revenue are harvested for the water company. Besides the commercial dimension of water losses, are the social costs to the people. High water losses mean many households are denied access to treated water or may have to contend with intermittent water flows and rationing. In the case of burst pipes, if they are not unattended

promptly, water users are likely to be served with contaminated water leading to health related problem. The government's intention in the contract therefore to ensure that non-revenue losses is reduced the pre-contractual rate of 48% to acceptable levels of 26%. Table 8.3 shows that between 2006 and 2011, the management of AVRL recorded non-revenue water losses of 52%, as compared to the 48% losses when the company took over the management of GWCL. The actual performance fell below the pre-contractual levels by 4 per cent points.

In addition, comparing the water quality summary in Table 8.5 from the Ghana Standard Board, a government agency responsible for the maintenance of acceptable standards of products and services, indicates that AVRL met three out of five water quality standards (GWCL, 2010). Two critical requirements, chlorine and E.Coli levels, are found to be higher than international standards allow.

**Table 8.5 Ghana Standard Board: Water Quality**

Standard parameters	Target number	Actually analyse	Complying	Analyse	Complying	Compliance index (0.95)
P <sup>H</sup>	13247	12965	12815	98%	99%	0,97
Colour (15Hu)	11967	11692	11477	98%	98%	0.96
Turbidity(5)	9487	8870	8560	93%	97%	0.90
R Chlorine (0,5 mg/L)	12944	12177	10956	94%	90%	0.85
E- Coli (ocf/100ml)	2461	2110	2107	86%	100%	0.86

Source: GWCL, 2010

It appears from the performance of AVRIL that the technical problem on the water losses was complex than was first thought. The major concern of AVRIL executives was that most of the pipes were old and subject to frequent bursts, and this became acute when some members of the public illegally tapped into to the main supply lines and left the water to gush out. In some cases, road construction works have led to pipes of the big mains and add to the problem of water losses. The chief executive of AVRIL (CEOW) mentioned that this was brought to the notice of GWCL management and the government for broken pipes to be replaced, but little was done about the problem.

In relation to the quality report, the CEO of AVRIL admitted quality failures but noted that they should not be interpreted strictly as 'failures'. The explanation is that AVRIL introduced cutting edge technology into detecting elements in water which gave more accurate data readings than before they took over the affairs of the company. He believed that if the new monitoring equipment was used in measuring water quality levels before they took over, the data would have shown that water quality had improved significantly.

Another area of performance that AVRIL was expected to achieve was to use efficient processes to achieve cost savings and improve the financial stability of the company. The researcher could not obtain financial reports for all of the relevant years from 2005 to 2011. The 2010 and 2011 financial reports were not yet ready to be audited by the Ghana Audit Service, Ghana's public expenditure watchdogs. However, despite these difficulties, we can build a reasonably clear financial picture from the interviews, company records and files.

In the case of financial performance, evidence from the interview shows that between 2005 and 2009, quantities of water sold dipped from 108.88 million cubic metres to 107.7 in 2008 112.3. In the same period, revenues increased from a loss of \$1.3million to a profit of \$2.4 million, representing an increase of \$3.7million (GWCL, 2010) indicating a strong performance based on water sold. The subsequent years from 2008 to 2010 continued to see the company recording profits in the books, even though it is difficult to verify their amount and accuracy since full access to the records and files during the research was denied.

In the absence of confirmatory data, we rely on the assurances given by both the managing director of GWCL and the CEO of AVRL that the water company did not record losses in the books. Based on that evidence it appears that AVRL executives increased revenues to the GWCL's accounts over the period.

Despite the fact that AVRL achieved some success in running the water company, two questions arise: whether those achievements represent an increase in financial efficiency and whether it delivered cost savings to the people of Ghana. The key indicator we can reliably use is related to the revenues lost to GWCL as a result of water produced but lost in transmission before reaching the consumers. The assumption made for the purposes of this analysis is that about half of these losses are preventable (ie non-revenue water losses). From this basis and comparing the percentage of water losses and accounting for other factors, it appears that the AVRL executives were not efficient. The basis for that conclusion is clearly indicted by comparing the percentage of the water losses before the contract was signed in 2006 and comparison of the minimum level expected by the government from the service provider and also with the the actual percentage achieved.



As seen in Table 8.4, data prepared by the GWCL shows that the pre-contractual level losses were 48% and AVRL was expected to reduce the percentage level to 26%. However, the percentage loss worsened, jumping by nearly four percentage points to 51.7%, indicating clearly that AVRL executives may have been inefficient. If we are to apply the losses to the 26% targeted, it is reasonable to state the missed target is wider which in turn, indicates that revenue losses to GWCL could have been even higher. Although it is difficult to quantify the water losses in monetary terms, we draw on the indications given by interviews, the press and World Bank reports.

According to the DCEO at GWCL, the estimated revenues lost to the company are over US\$50 million during the same period. His estimates are based on average water tariffs applicable at the time. Further evidence came from the corporate affairs manager of AVRL. In an interview granted to a newspaper on the performance of reducing non-revenue losses, he estimated the non-revenue losses to be over US\$100 million annually (Public Agenda, 2009; All Africa, 2009). Similarly, the World Bank report (2011) authored by Foster Pushak, gave a conservative figure of US\$56 million loss per year. The above estimates coming from independent sources clearly give us a good idea of how much savings could have been made. At least, 80% of the amount could have been saved.

Although it is possible for AVRL executives to blame the government for not providing infrastructure support, is challenged by the GWCL evidence that four more dams were constructed, leading to an overall increase in water production. Based on increased water production, revenue should have been increased well above what has been reported in the books.

### **8.3.2 Cost of Operations**

The appreciation of the cost of operations from data obtained from the company shows that the unit cost of water production continued to rise steadily from the 2005 level, with 66% increase by 2009 while unit revenues increased from 55.90 in 2006 to 106.6 in 2009, representing 91%, and cost per unit increased by 66% from 54.32 unit cost to 90 unit cost in 2009, suggesting that more costs were incurred in running the company. In other words, the AVRL appears to having failed to make cost savings for GWCL. From the above analysis it is evident that the financial performance was sub-optimal, given the amount of savings that could have been made.

Although there might be some challenges in water production resulting in poor financial performance, the explanation lies in the fact that the service provider had less incentive to adopt value adding measures to bring water losses to the level desired by the Ghanaian government. There are two possible reasons for this. Firstly, AVRL is given a guaranteed income irrespective of performance. As a result there is no compelling reason to adopt value adding process to minimise water losses.

Secondly, the government did not have sufficient leverage over AVRL executives to run the company as it had expected, especially when incentive structures in the partnership were weak. This is in line with power expectation since AVRL is highly dependent on AVRL. From these perspectives, it is likelihood that the suppliers will exploit their power advantage to hold the government and perform below average.

It is also possible that the AVRL indirectly is influencing the poor results by not adopting the appropriate value adding approach. All the above suggests is that AVRL had the ability to decide how much of the revenues go to GWCL account. The point that stands out clearly is that the government is powerless to act when access to the books is restricted, providing further indication that AVRL is dominant and the relationship is adversarial collaboration. In that situation, and going by power-dependency theory, AVRL performance will fall below expectation.

The other issue worth considering relate to information asymmetry making it difficult for GWCL to know whether the poor performance is opportunistic way to increase its returns. The contract made the service provider a sole operator of the accounts of GWCL. Although the idea can be justified on the grounds that the incoming AVRL executives needed free hand to introduce their brand of financial management into GWCL management, the problem for the government is that it does not have sufficient leverage to force the service provider to practice open book systems and transparency. This increases scope for moral hazards in the relation since information asymmetry makes it difficult for the government or GWCL management to know whether such attempts are opportunistic way to increase its returns

There are two ways this can occur- either through cost padding or under reporting revenues collected. Firstly, cost padding may occur because cost disbursements are done without any form of control and in the presence of cost uncertainty, GWCL will not be able to isolate the AVRL inefficiencies or differentiate AVRL personal expenses from that of company. Given that AVRL is in business to maximise its returns from the relation, it has incentives to pass on their inefficiency to GWCL if this could not be detected. .

Secondly, under-reporting revenues will be difficult for GWCL management to detect since access to the books is restricted and the only access to information about the water company is through the financial reports issued by the financial auditor at year end. Since it is difficult to determine the maximum cost to be incurred every month and minimum monthly revenue to be possibly generated from water commercial activities, it is reasonable to expect AVRL executives to have incentive to over exaggerate cost and/or under-report revenues, and appropriate the same for its own benefit.

When the post-contractual moral hazards are combined with the guaranteed income, which may have contained economic rent, it is reasonable to conclude that AVRL was appropriating rent from the relationship. The results also show that GWCL management or the Ghanaian government had not considered the possibility that the service provider would exploit this arrangement, taking advantage to increase its returns from the relationship.

In summary, the above evidence on supplier performance indicates that the GWCL received reduced functionality and increased operating costs while the AVRL executives were managing the water company. On the other hand, if there were any cost savings, it is not clear whether these were passed over to GWCL. Nevertheless, any of this behaviour is likely to occur when a particular supplier is dominant and the buyer does not have sufficient power resources to enforce contractual performance or to compel the service provider to pass over cost savings. This warrants further careful examination since it supports a case of hold up or post-contractual imbalance in the relation.

This form of supplier exploitation can occur especially when the supplier is dominant and possibly holding-up its obligations in the contract. As we observed under the post-contractual balance analysis, since the service provider is irreplaceable, at least in the short run, and the transaction involves essential public services, the supplier may exploit its power position to force the government to take on all risk and uncertainty. In addition, the supplier created high switching cost for the government through the sovereign guarantees and the government become dependent in the relationship.

The analysis presented here on evidence of post-contractual hold-up and rent appropriation comes with a problem. A variety of reasons may affect supplier performance that may not arise from opportunistic behaviour or shirking and this may include conditions that go beyond the supplier's control. Similarly, if the hold-up occurred, it does not mean that economic rent was appropriated during the contractual period and as already noted in telecom case, may be due to other reasons (Klein, 1996; Coase, 2006). For example, a supplier may not be opportunistic and is committed to the principles of genuine partnership and reciprocity or a supplier may not be aware of its power situation and exploit it. Therefore it is difficult to conclude in this case that AVRL's behaviour demonstrates that it appropriated economic rent. A similar observation can be made on the buyer side. The GWCL officials found it difficult to determine whether claims of rent capture occurred, presumably because they could not access the books to review the cost base and earning margins of AVRL as compared to standard benchmarks.

In sum, when considered against the adversarial collaboration witnessed in each of the contracts with the service providers, we can reasonably conclude from the available evidence

that the adverse pre-contractual weakness of the Ghanaian government contributed to it failing to get good supplier performance and good value for money in the telecoms and water contracts.

#### **8.4 Concluding Remarks**

In this chapter, the impact of the adverse post-contractual balance on supplier performance has been explored. This is based on the hypothesis that when a public sector body is not able to develop a balanced relationship with the private sector, it will be difficult to get the best performance from the supplier.

This is an interesting research problem that potentially has applications in many other areas in public management and private businesses. According to new developments in the world of businesses, risk incentive contract design is being adopted to manage risk and uncertainty consistent with agency arguments (Jensen and Meckling; 1976; Holmstrom, 1979; Eisenhardt, 1989). This is even more problematic for the government of Ghana when the transaction involves essential services having social, political and economic implication for the government.

The less than the minimum performance from two suppliers can be explained by the post-contractual power relationship they enjoyed in the relation. On the supply end of the market, as the two suppliers enjoyed near market monopoly status became very powerful in their own right took advantage of their power advantage to dictate the terms of the contract. In line with

the resource dependency model (Emerson, 1962, Pfeffer, 1978) pre-contractual bargaining power is a function of the relative utility and relative scarcity of the resources each party brings into the a particular transaction. This means that the two service providers will have more bargaining power and be in a favourable position to dictate the terms of the contract by forcing the government to take all risk upfront.

The poor performance of the two private service providers can also be attributed to the fact that they had a credible promise from the government on their future guarantee income. As a result, there was no incentive on the part of the suppliers to put in effort to achieve their minimum performance.

Other factors like political risks also worked against the government of Ghana in both telecoms and water transactions. The political risk concerns in international business collaboration raise the possibility of sovereign guarantees, which force the government to take on more of the risk and uncertainty (Woodhouse, 2008). In both cases, the sovereign guarantee instrument created high switching costs and lock-in effect for the government. Thus the post-contractual bargaining power was weakened and the option to exercise its rights of exit became academic exercise even if the government is no longer benefiting from the collaboration in the face of opportunism. This is amply demonstrated in the empirical study of the two contracts.

One important obstacle is one related to the government's responsibility in providing vital services and adversarial collaboration. From government's point of view, although the performance of the two suppliers was below expectation the government had to work

collaboratively with the two service providers. The government may have reasoned about the implication of exercising its option to sanction the supplier or change suppliers. However the government faced formidable obstacles. First is the scarcity of the suppliers, switching costs.in order to ensure that public vital services were not disrupted by the process of tendering and award of a new contract, which would also incur switching costs. Based on this reasoning, it could be reasonable to argue that the government may have found it beneficial not to change partners and may have allowed the service providers to appropriate majority of the surplus value or economic rent, rather than incur high switching costs to seek another supplier.



## **Chapter 9**

### **CONCLUSIONS AND CONTRIBUTIONS**

#### **9.1 Introduction**

This final chapter of the thesis concludes the study that investigated the arguments empirically that the adverse pre-contractual power relations will make it difficult for the public sector to achieve balance with the private sector. The major findings are highlighted and are followed by discussions, contributions, limitations and future research areas.

The chapter is organised as follows Section 9.2 restates the purpose and objective of the research. Sections 9.3 summarises each case and findings. Section 9.4 discusses the findings Section 9.5 provides contributions to theory, practice and limitations. Finally section 9.6 makes suggestions for future research.

#### **9.2 Purpose of the Study and Hypothesis**

The Public-Private Partnership (PPP) policy has been practised by many governments in developed countries over several decades in the delivery of infrastructure and service provision, notably in the UK, USA and Australia.

In the developing world, recent reports released by the World Bank (2011) showed that governments in developing countries are increasingly being encouraged to adopt PPP policy with the principal aim to allocate and share risk to the private sector in a mutual satisfaction fashion (Ainuson, 2009; Larbi, 2008; Ahadzi, and Bowles 2004; Akintoye et al. 2003).

Whilst many writers have argued that there have been tremendous benefits to governments from PPP policy, it has also generated much criticism over claims that PPP-run projects have actually cost the taxpayer more than the traditional public procurement approach and that governments have failed to transfer risk to the private sector. This dissertation has covered a number of important theoretical and empirical issues relating to these arguments on risk transfer and post-contractual balance in PPP. Given the complexity of the PPP policy and its implementation in general, coupled with the fact that there is no single theory in contract design, theatrical discussions were drawn from agency, PRT, TCE and power dependency theories. In addition, theoretical insights were also drawn from strategic management literature with emphasis on contract management. Thus the theoretical insights allow us to evaluate the theoretical and theoretical underpinnings pertaining to the Ghanaian case.

The product of the literature reviews from TCE and resource dependency theories resulted in a key research question whether the Ghanaian public sector authorities have the ability to develop post-contractual balance and also good supplier performance. Two hypotheses were constructed from the literature and consistent with Lonsdale model Lonsdale (2005a). The first hypothesis is that: ‘Adverse pre-contractual power relations, asymmetry in negotiating resources and capabilities, are likely to make it difficult for the Ghanaian public sector to achieve post-contractual power balance with the private sector as prescribed in transaction

cost theory.’ The second hypothesis ‘Lack of post-contractual balance would result in poor performance outcomes by the supplier’ was constructed. This study used qualitative case study design for the investigation.

### **9.3 Summary of Findings**

In the first PPP case between GT, a Ghanaian public telecommunications company and its private sector partner TMP, results showed that the first hypothesis is supported. This is interpreted as adverse pre-contractual power relation, asymmetry in negotiating resources collectively and significantly impacted on the ability of the Ghanaian public sector to develop post-contractual balance in the relation. The second hypothesis that post-contractual imbalance will lead to poor supplier performance was also supported. In the second case, findings showed that both the first and second hypotheses were supported.

Both GT and GWCL companies although contracted in different time periods shared common features of pre-contractual power and hold up problems. Specifically, both companies became vulnerable in terms of its transaction salience of the contracts, high supplier scarcity and information asymmetry. These factors created power asymmetry and a subsequent dependent relation on the service providers (lock-in). In relation to the other independent variable, the study found that both companies failed to raise competent negotiation team and pursued narrow political agenda. Although we found the link between the second independent variable to suppliers’ hold-up (lock-in) weak it nevertheless made it difficult for public authorities to design balanced contractual terms with the private suppliers.

With regards to supplier performance, post-contractual weakness of the Ghanaian public sector authorities made a big contribution to it failing to get good supplier performance and good value for money. In the GT contract, the government failed to get the supplier deliver the minimum number of telephone and internet connectivity to designated areas. In the water sector, the government failed to get the non-revenue water losses reduced from 48% to 26%. On the contrary, the water losses worsened recording nearly 52% at the end of the contract..

## **9.4 Discussions**

Although PPP policy is an important mechanism for the delivery of essential services for governments in developed countries, particularly in the UK, the USA and Australia, and a large amount of research on this has been undertaken, the problems affecting its successful transfer of risk are largely unknown. One of the problems around PPP policy that has intrigued policymakers in the public sector is why the good intention to create a mutual inter-dependent relationship and the transfer of risk to the private sector has not been entirely successful. While it may be possible to design an efficient contract, sharing risk with the private partner, as suggested by TCE, it is not clear whether the public sector has the ability to achieve that objective. The problem is power. It has been typically argued that the public sector is often affected by an adverse pre-contractual balance given the imbalance in the distribution of critical resources with the private sector. This is because the essential nature of the services performed on behalf of government partly account for the problem. While the literature is focusing on transferring risk to the private sector little attention has been paid to the constraints to efficient risk transfer. However, the real beneficial outcome of PPP for Ghana's government will depend on the lessons learned from the two cases and the challenges being appreciated and appropriate strategies adopted in future PPP transactions.

Against this background, this research has provided important insights about the problems of using PPP in public provision.

The two cases that have been examined empirically in this study form part of the widely practised procurement policy of using the private sector to provide key public services on behalf of government. Both scholars and the World Bank had argued that private sector suppliers are more efficient in managing public utilities by bringing improvement in public procurement activities through risk management. As a result, the Ghanaian government was prevailed upon to form collaborative partnerships with the private sector aimed at benefiting from increasing functionality at reduced cost to the taxpayer. The two cases were examined for specific evidence and the results presented interesting insights into both knowledge and practice.

When comparing the two cases some major similarities emerge. Both GT and GWCL are publicly controlled utility companies providing essential services in telecoms and water supply services, and both projects funded by World Bank loans. The empirical study provides evidence that there has been some measure of success in the two cases, including staff training, extension of telephone and internet services to schools and colleges, and installation and extension of water supply services to the people of Ghana. More importantly, TMP, the private sector partner in the telecoms contract, turned the loss-making GT into a profitable telecom company.

Beyond that, the actual performance fell below the minimum performance required by the government in both contracts. As a result of adverse pre-contractual power relationships, arising from high utility (essential services), supplier scarcity and information asymmetry, post-contractual dependence was created for the government. This made it difficult for either GT or GWCL to leverage their international suppliers for enhanced performance. More significantly in the two cases, despite the level of commitment shown by the government in both contracts, the relationships can be best described as adversarial collaboration in which each of the suppliers were in dominance position. In addition to threats of withdrawal and high switching costs created by sovereign guarantee bonds, the government could not develop the relationships into two-way collaborations, because there was little scope left open to create this situation.

The review of the post-contractual imbalance problems as evidenced in the two cases highlights some important strengths and shortcomings of most existing theories on contract design. The results found support for resource dependency theory, that the ability of the public sector to control PPP relationship is dependent on its ability to obtain key power resources in the relationship (Hingley, 2005; Pfeffer and Salancik, 1978; Cox et al., 2001).

The results of this study complement prior studies that show that rent appropriation depends on power. This suggests that in circumstances where the public sector is in relatively weak power position with the supplier will not create opportunities to leverage the suppliers to deliver continuous functionality and cost improvements. Thus the attitude of the Ghanaian authorities in not considering these power dynamics in their relationship with the private sector suppliers is simply demonstrated in the two case contracts. This can be explained by

the lack of appreciation of the profit motive of the private sector when they enter into business relationship and that suppliers will exploit asymmetrical lock-in to perform below expectations even if the buyers in control of the relationship (Cox et al., 2003; Hartley and Parker, 2003). This clearly had an impact on their ability to support the appropriate governance structures to minimise their vulnerability to hold ups and opportunism.

This study also draws attention to one area that must be understood in the context of contract design and is related to contracting in specialised and restricted markets. Contrary to liberal economists' thinking that the private sector model encourages competitive bidding to wipe away rents from contract pricing, this study found that this is not always the case in PPP transactions. In a commodity market, where many suppliers exist, buyers are able to use market competition to drive prices down. However, in the public sector, such as water and telecoms industries most of the projects are specialised in nature, with few qualified specialist suppliers. As a result of the high entry barriers, the few specialist suppliers in the industry tend to enjoy non-competitive market power and may engage in monopolistic pricing. In the two cases examined the problem of supplier availability is compounded by the industry both the telecoms and water contracts are located and the essential services run by the two companies (see also Ainuson, 2009; Hall, 2003). In the absence of alternative suppliers, the relationship was transformed into a dependency and a lock-in. This aspect of findings about critical resources being the cause of lock-in is significant. Although asset specific investments have played as a major cause of lock-in in TCE analysis, this finding is complementing other studies that critical resources with no alternatives can create lock-ins (Cox et al. 2001; 2002).

In relation to the second independent variable, i.e negotiation resources and capabilities) the results found some support that inferiority of Ghanaian negotiation team in respect of resources and capabilities allowed the public sector to be outplayed by the private sector sales and negotiation team. In terms of lock-in, findings do not find a strong support that it directly contributed significantly to the lock-in that occurred in the two cases. However, support was found in terms of the inferiority of the negotiation that negotiated on behalf of both GT and GWCL was outsmarted by the well-prepared and resourced private sector negotiators superior. In this respect, the findings from this study complement the recent PAC report (2009), and also relating to Lonsdale's (2005a) earlier discussions on the superiority of the supplier's sales and marketing team over the buyer's procurement team that the public sector often find itself outsmarted and outplayed.

Useful lessons can be learned from the case and proactive measures could be taken to build the capacity of the negotiation team. Furthermore, given the adverse pre-contractual power relations of the government in the two contracts, it is doubtful even if a competent negotiation team might have struggled to get a better deal. Even then, neither the telecoms nor the water negotiation team could be described as competent, as members of both negotiation teams had no prior training or experience in commercial skills. It could be pointed out that although the new Ghana procurement law has brought about some improvements in strengthening the functional capacity of the procurement department, the Ghanaian government needs to do more to improve the independence and capacity of the agency to perform its watchdog role.

In relation to supplier performance, the results found strong support for the proposition that if the post-contractual balance is in favour of the supplier, the buyer will find it difficult to get



the supplier to deliver functionality and cost savings. The results are consistent with theory: when the buyer is dependent on the supplier, the supplier will exploit its dominance to reduce level of performance and extract rent from the relation. Findings also complement TCE assertion that actors in misaligned governance structures are not likely to the best performance from suppliers (Williamson, 1985; 1991). This suggests that buyers in post-contractual balance in a relationship have many opportunities to leverage the supplier for optimum performance in the area of functionality and efficient cost delivery than when in adverse post-contractual balance. This point is stressed by Cox et al. (2003;2004) re-echoed in Lonsdale's study (2005a; 2005b) and is related to adverse power relations reported in other studies, for example the 'Libra IT project; NSI and SBS' (Lonsdale, 2005a).

However, the result is not consistent with TCE optimism about the ability of public buyers to balance their relationship with the suppliers using credible enforcement commitments in the presence of risk misalignment. Williamson holds the expectation that buyers are farsighted enough to anticipate contractual hazards, and have the ability to select the most appropriate efficient contract that will force suppliers to take risk extra-safeguards to ensure that suppliers deliver functionality and cost savings (Williamson, 1983). The findings from the two cases also challenges Williamson's reasoning that competent buying managers should be able to ensure that risk in the relationship is equitably shared with suppliers.

However, the results of the two cases suggest that credible commitments can only be implemented under circumstances where the buyer is in inter-dependent relationship or dominant. If the buyer is in a dependent relationship, it will be difficult for the public sector manager to force the supplier to accept taking more risk. This limitation on the part of the

public authorities challenges TCE's assumptions on the public sector unlimited foresight to select the most optimal contract design for a given specific transaction. Williamson also did not explain what it is that the buyer may not have the ability to leverage the supplier for efficient performance. This thesis has demonstrated that power structure may explain why the buyer may not be able to balance the contract in the manner prescribed.

This insight challenges much of the TCE assumption that tends to suggest that power is not relevant in the business-to-business market because the parties are equally matched in terms of resources. This research has shown, contrary to Williamson's view, that asymmetry in the resource endowments of exchange partners is equally as powerful as asymmetry in asset specificity in shifting a relationship from balance to post-contractual imbalance.

The weakness of applying TCE reasoning also brings into focus the agency model and its prescribed incentive structures to influence supplier behaviour (Holmstrom, 1979; Jensen and Meckling, 1976). Although the Ghanaian authorities did not consider this possibility and failed to manage uncertainty in the telecoms and water contracts, it has been demonstrated in this empirical work that this was a fundamental error in judgement. Given the level of uncertainty and information asymmetry in the two cases, and the absence of a risk incentive structure, it is not surprising that the government obtained poor supplier performance.

The result of this study suggests that external factors related to political and property risk impacts could also partly explain the difficulties that governments face in achieving post-contractual balance. In addition to the key problems mentioned above, the study draws

attention to external financial and political contextual factors as additional dimensions to the problem of achieving balance for governments in developing countries. These are related to the World Bank project financing role and political risk dimensions which were not identified by the Lonsdale study and have also received little attention in the literature.

The results of the two cases independently show that the World Bank project financing requirements contributed significantly to the weak bargaining position of the Ghana government thus affecting its ability to leverage its suppliers to accept risk for better performance. In particular, World Bank's role indicates that little attention was paid to the possibility that international suppliers will frustrate contracting governments in the areas of risk sharing and efficient contract design. As found in the two cases, suppliers exploited the influence of World's financing leverage to their advantage. In this context, this study complements other studies that World Bank does not make an attempt to specify or explain how private participation would generate an outcome that would yield the highest benefit to the host country (see Bayliss and Hall, 2002; Lobina and Hall 2003; Kessides, 2004). As a result, this study advocates for World Bank to take a critical look of its financing policies again and work out proactive strategies that will support genuine partnership between the public and private sector.

Flowing from above is the issue related to sovereign guarantees which is tied to the issue of political risk. As we noted in the two cases, sovereign guarantees for all intents and purposes are similar to financial hostages, as defined by Williamson (1983) in his credible commitment model aimed at providing assurance to investors of the security of their investment. However, this approach resonates well with property rights theory that prescribes that the party who

manages, say the governments with weak property rights regimes should be made to bear a larger proportion of investment risk in transactions (Oslo, 2000; Williamson, 1991; North and Barry, 1989). However, the downside of it as demonstrated in the two cases is that the service providers were able to use that to create high switching cost for the government and effectively locked the government permanently in the relation. The implication is that it rather pushed the government into high levels of dependency with the effect that the government's aim of transferring risk to the private sector companies is frustrated by its weak position with the suppliers. This observation is borne out of the two cases and concurs with Hall's (2003: 13) assertion that sovereign guarantees demanded by international service providers are contradictory to the principles of risk transfer and sharing; namely, their capacity to take on *risk*. He argued in his report *On Water Multinationals* that, "multi-national guarantee is a country's risk, which can be translated into a huge financial burden at an unexpected moment... countries should be advised to ignore invitations to give guarantees in order to entice the multinational companies". It could also be added from the empirical study that this makes the contracting country highly dependent on the goodwill of international suppliers (See also Woodhouse, 2008). This implication of political risk to policy makers means that this dimension should be considered in analysing the contractual problems of PPP in developing countries.

## **9.5 PPP-Management Contracting**

One further issue concerning the management contracting of PPP must be understood: the issue as to whether this form of PPP helps the public sector to transfer risk to the private sector. Our research may shed more light on the conflict of interest in the management contracting form of PPP which is widely practised in many developing countries (Saussier,

2004; Iossa, 2007; Barlow and Koberle-Gaiser, 2008). This relationship between the buyer of the management services and the service provider raises the possibility of post contractual moral hazards (Cox et al., 2004) as a result of information asymmetry. As was observed in the two cases, a supplier may have incentives to under-perform and attribute the problem to category factors beyond its control. In this regard, one would expect, based on uncertainty arguments, that risk incentive trade-off should have been adopted, given the difficulty of monitoring the service providers. This insight resonates well with Holmstrom (1979) who addressed the trade-off between risk and incentive and noted that the importance of applying risk incentive trade-off is to treat the relationship as an agency problem.

## **9.6 Contribution**

In putting all the above analysis together, although PPP policy is an important public procurement strategy and has been practiced for a while in the developed countries and despite the amount of research done in the area, the contractual problems and its effect on efficiency outcomes remains unexplored. This research has found that the PPP can be analysed from three theoretical perspectives. Firstly, PPP policy implementation comes with high levels of uncertainty because the private sector performing on behalf of government essential services and that necessitates that risk incentive schemes should be considered. Secondly, incentive structures are important consideration in PPP since the transfer of public service provision to the private sector involves uncertainty in the level of efforts to accomplish a given task. This means that risk incentive scheme should be crafted into the contract design to minimise monitoring and moral hazards cost. Thirdly, property rights matter, at least in the developing countries context. Fourthly, transaction cost is important consideration because taking in-house activities to third party requires explicit instead of

implicit contracting. In the case of the PPP transactions, the transaction cost for the public sector includes tendering, writing contract documents, monitoring and enforcement. In addition, although TCE has made strides in providing guideline on how anonymous parties can design efficient balanced contracts, consideration of how parties can achieve cost minimisation objectives against the backdrop that power resources of utility and scarcity parties are not equal, has not been explored. With these issues considered, the thesis makes contribution to knowledge and practice.

### **9.6.1 Theory**

First, the analysis carried out in this research complements and adds to the growing body of literature asserting that both power dependency theories and incentive contracts theoretical model should be used as an either alternative or complementary theoretical explanation for post-contractual imbalance in PPP bilateral governance. As this study has demonstrated, although TCE analysis is useful in providing understanding of the contractual problems such as those in PPP, it also ignored some of the complexities involve in public sector organisation and the private sector. As a result, TCE provides partial contractual solutions to prevent post-contractual risk in partnerships. In the early development of the bilateral contracting model, Williamson (1985: 76) acknowledged that ‘Bilateral structures have only recently received the attention they deserve, and their operation is least well understood.’ In order to provide a deeper understanding of bilateral governance structures such as PPP and its complexities, other perspectives of power, agency and PRT theories can help in this direction. This point also adds to many empirical studies reviewed in this thesis. For example, Heide and 1988 Cox et al., 200; Sanderson, 2004; Lonsdale and Watson (2007) support TCE theories in understanding contractual problems they also complement their studies with power and

dependency theories. Similarly, Watson (2004) combined incentive theories with transaction cost theory to study the contractual problem in the film industry and the result is that a better understanding of managing risk with incentives contract design is provided.

Furthermore, the Lonsdale study was based on the UK public sector; the present study extends this generalisation into the developing country context, showing that power is important consideration in the crafting of incentives and extra-safeguards against post-contractual hold ups and opportunism. Beyond finding support at least, for the pre-contractual power relations, this study expands on Lonsdale's (2005a) study and extends knowledge by showing that the political risk, the World Bank and its conditionalities and sovereign guarantee, to which previous studies in PPP have paid little attention, should be considered as part of PPP analysis in developing countries. This is an important contribution, since these factors are commonly observed in international PPP contracting in developing countries. This is the first time their relevance has been highlighted as some aspects of impediments to the developing of post-contractual balance.

Finally, to the best of my knowledge, this study is the first to use the power model to explore the impediments to balanced bilateral balance in Ghana, as a developing country context.

### **9.6.2 Contribution to Practice**

The present study has contributed to practice with an analytical tool to assist public sector managers and policymakers in measuring and determining the possibility of developing a post-contractual power balance. An obvious shortcoming in TCE as a framework for

managerial decision making is the absence of coherent framework for determining when the public sector is likely to develop a successful post-contractual balance with the private sector. This research should be seen as complementing other power models on relationship styles for value capture (see Cox, Ireland, Lonsdale, Sanderson, Watson (2002). The power model proposed in the present study should assist public procurement managers to measure the power structures in their relation with the private sector and to choose appropriate risk-incentive contract design to manage risk in their relationship with private suppliers.

In relation to management contracting of PPP, this study contributes to the understanding of the challenges and problems that are encountered when the public sector contracts private management services to perform essential services on its behalf. Findings from the above case suggest that moral hazards may be high in such contracting environment. This study therefore should be seen as timely revelation of the risk so that proactive remedial action such as the use of risk-incentive schemes could be crafted into the contract design to protect the public sector from post contractual moral hazards.

Lastly, this study serves as feedback to policy makers in Ghana and those at the World Bank Secretariat for improving strategic policy towards PPP initiatives for efficient outcomes, and the Ghanaian authorities for improving implementation of PPP-run public projects. To the Ghanaian authorities, this empirical study has provided an analysis of data collected from top executives the public sector and the private sector, the World Bank and politicians using well-crafted semi-structured questions to illicit the right responses on problem of designing efficient contract and extra-safeguards. As a result, this study provides valuable insights on contract management under PPP to the benefit of Ghanaian authorities. The research helps



explain the various problems that future PPPs face and the challenges posed when attempting to get the best deal from their international partner suppliers. Similarly, this study will be of tremendous help by bringing into the open the importance of designing strategic frameworks for PPP in the country to harmonise resources and minimise their vulnerability to supplier opportunism.

### **9.6.3 Recommendations for Improvement**

On reflection on the research, a positive observation can be made about PPP. Ghana has enjoyed some benefits from the private sector model: at the very least, the private sector has helped the government to keep these two vital public services in uninterrupted operation. Although there are problems for the Ghanaian government associated with the private sector model in the context of balance and risk transfer, there are ways to improve future PPP transactions in the country. As a result, the researcher makes the following recommendations:

(1) Given the gap between the public sector and the private sector making it difficult to match the experience and negotiation competency of the suppliers' teams, it is necessary to raise an experienced government negotiation team. To strengthen the capacity of the negotiation team, it is necessary to create a central and autonomous institutional body, to handle high-level procurement contracts with international suppliers.

A national strategic PPP policy framework should be created that reflects cost-effectiveness and timely project execution. Such a framework will not only help streamline procurement procedures in contract award, but would also minimise suspicion of corruption on the part of political authorities who negotiate on behalf of public sector bodies.

(2) Establishment and training of a dedicated department responsible for public contract negotiation with foreign companies within the public sector instead of ad hoc teams. This would enable the established body to build resources, capacity experience in order to negotiate with the private sector on equal terms.

(3) To facilitate the above independence and minimise political interference, public institutions and structures should be strengthened in order to play their watchdog role. In this regard, monitoring and enforcement mechanisms should be put in place and given political support. For example, the National Audit Service and parliament should be resourced and supported to carry out their constitutional mandate of keeping watch over public expenditure, and public officials found engaging in fraudulent, corrupt procurement practices must be prosecuted.

(4) A transparency-based system including processes, procedures and decisions to hold partnerships accountable should be encouraged. For the system to work effectively, it requires that managers be free from political patronage and influence.

(3) There must be a deliberate policy targeted at indigenous Ghanaian public sector entrepreneurs, encouraging them to participate in national infrastructure and service delivery.

## **9.7 Limitations**

The international context of our study has shed light on the nature of various aspects of impediments to post-contractual balance in PPP initiatives. Despite the meticulous approach used in gathering the data and the rigour of the analysis thereafter, there are some notable limitations to this research which might necessitate further investigation. These limitations

relate to the cases examined and the difficulties in operationalising the first and second independent variables.

The first limitation of this thesis is that the study used only two public sector organisations as case studies: one in the telecommunications sector; the other in the water supply sector. These two organisations are large enough to offer an appropriate platform with which to test the hypothesis. As noted by Yin (2003: 10) ‘case studies, like experiments, are generalisable on its theoretical propositions, and not its populations or universes’. However, the generalisability of the results could be made more robust with further studies in other countries in the developing world. In the context of this case, the study use of two cases from one country cast some doubts on its generalisability to other developing countries.

The second limitation of this study concerns the data collection. The analysis of the telecoms contract was based on interview evidence and historical data covering a period between 2003 and 2006. Although the contract was quite recent, much of the data was either destroyed or lost when the company was finally sold to Vodafone UK in 2008. It also became evident that some documentary evidence was considered too sensitive to be released to the researcher. Although this problem was addressed by interviewing the managers who served as deputies and some of the TMP staff, there is a possibility that the researcher might have missed some key information which may have impacted on the conclusions reached.

Although care was taken to ensure data integrity, it may suffer from evaluation apprehension bias from informants (Cook and Campbell, 1979). This refers to a situation whereby the quality of the managers’ responses might be limited either by their ability to recollect from memory, or being influenced by the role they played in the transaction, leading them to be

selective in their responses, in order to put them in a good light. However, the potential effect of this issue on the conclusions is minimised by the triangulation of interview evidence, other data and the government's ministerial report on the GT sale which covered the tenure of the TMP management process and procedures, a copy of which was made available to the researcher.

In the case of the water contract, data was collected in February 2011, when the contract was still on-going. Although care was taken to obtain all relevant information from both the interview and documentary sources, there is a possibility that new evidence has emerged between the period when the data collection for this research ended, and when the contract finally came to an end in June 2011. Although feedback from the company indicated that the contract was not renewed because of the poor performance of AVRL, further research would be needed to thoroughly examine the changes in the pre-contractual power resources between the two partners in the intervening period.

An additional point worth mentioning is that the robustness of the results can be affected by the qualitative-based indicator method chosen for the operationalisation of the variables for the second independent variable. The indicators used for the measurement of the second independent variables are based on aggregations of indicators from a number of sources such as surveys carried by Karass (1994) and Lacity et al. (2009). While these indicators were identified in the data and analysis, precise qualitative measurement are crude measures for these variables and may not capture every aspect of the problem. For example, we relied on the assumption from the literature that the supplier's marketing and sales department is better resourced with superior capabilities and it is the task of the public sector procurement

department to match those attributes or miss getting a good deal from negotiations. It is significant to sound a note of caution here that the fact of a negotiation team having the appropriate attributes does not itself mean that it can achieve its objectives during the bargaining process, since other factors might compromise the bargaining process that this study was not able to capture or ignored, which could otherwise have given different interpretations and results. In other words, although we successfully examined the effect of asymmetry in negotiation, and resources and capabilities as they relate to post-contractual balance, the model could not fully explain their impact on the pre-contractual balance. The imperfect measurement accounts for the weak link, given that this study is internationally related. As a result, this study does not claim to have dealt exhaustively with the measurement of the agency variables.

In relation to supplier performance, two aspects of the conclusion reached by this study need to be considered with caution. The first is the conclusion that the two suppliers in the two contracts failed to deliver on their contractual promises. There could be problems with such conclusions when it is they are based on the limited data available to the research. It may be that there were some hidden intervening problems, process and procedures that would have affected the performance of the service providers. For example, the political and investment fund support from the government might have been low and that had the potential to affect supplier performance, because the supplier was working with less infrastructure and resource support. This was pointed out by the service providers during the interviews that the government did not provide all the necessary supporting infrastructure investments which would have improved their chances to fulfil their contractual obligations. Alternatively, it is also possible the pre-contractual outcome targets set for suppliers might have under-estimated the enormity of the problem, or the government did not make full disclosure of the problem

during negotiations. Any of these factors could have affected the outcome of the supplier's performance. Hence we must remain cautious in our conclusion that the supplier's failure to deliver on their promises was deliberate or solely attributed to the supplier.

### **9.7.1 Future Research**

This work is the first study on Ghanaian PPP to examine constraints to post-contractual balance. Although the strength of the model developed to examine these factors and the picture built from the research reflects as accurately as possible the perception of the interviewees, there is room for further research into areas not sufficiently dealt with in the study.

The relationship between negotiations resources and capabilities and post-contractual balance has been addressed by this study. This could be considered as a sincere attempt to investigate their relationship, but it is not dealt with in depth. Related to this is another dimension of internal politics which was included in the Lonsdale model but was not examined in this thesis. While organisational politics reflects among other features lack of argument among organisation members, especially about respective goals (Pfeffer and Salancik, 1978), the boundary of its activity with resources and negotiating capabilities are blurred with regard to activities around policy contract negotiations and implementation. For that reason, a study of internal politics at a political leadership level should prove a promising way to see how that impact on decisions to implement PPP policy in a country. The fact that the government hastily assembled the two negotiation teams on each occasion, accompanied by pressure to conclude the contract without being given the freedom to thoroughly examine the supplier's

draft proposal, gives the impression that the PPP decisions are also political choices in developing countries taken at the top level of the political power structure. There is evidence that the executive power of government routinely by-passes procurement professionals when negotiating with international bodies (Aunison, 2009; Amin, 2007; Larbi, 1998). Although such work may be difficult, given the political nature of the research, it will enable us to gain a richer appreciation of the various impediments to optimal contract negotiation. We hope that future research will look at the full picture here. Although such work might be involving and challenging, it will produce a deeper and richer knowledge than could be achieved in this limited research study.

Another consideration deals with the increasing role of the World Bank. It is clear that the World Bank is the major sponsor of PPP in developing countries in terms of infrastructure development. Such intervention puts political pressure on governments to make political concessions to suppliers. However, working with international suppliers with high standards of project planning and investment modelling could even encourage the political authorities to make far richer decisions with measureable outcomes than was possible for them in the past. While this assumption has not yet been examined, future research should pay attention to this possibility.

Lastly, the qualitative study was useful approach to identify and describe the causal relationships between the two independent variables in post-contractual balance. However, these methods may not be well suited for establishing a quantitative relationship and the measurement of the supplier's performance. A possible bias could arise from the method of used in the measurement problem of comparing the achieved performance and the pre-

contractual target set. To avoid the limitations of the qualitative study, future research should use quantitative measures in order to prove the direct relationships between the independent variables.

Although evidence of the effects of bargaining competencies was found, their direct link to lock-in or hold up is weak. A further observation to be made is related to the role of the political leadership interfering in contract negotiation and management. Little is understood about the implications of this interference, together with all of the political choices and social and cultural issues that could be seen to have an effect on contract design and supplier performance.

Future research should study these issues and build models to look at their effect as well as other dimensions of external factors such as political risk and World Bank financing policies on PPP projects as they relate to the question of the pre-contractual bargaining power of host countries with the private sector. More importantly, more research in both developed and other developing countries will allow us to identify other factors that may be likely to affect the development of balance in PPP relation. Although such work may be difficult, it will enable us to produce a richer appreciation of the various impediments to optimal contract design in PPP contracts.

### **9.7.2 Concluding Remarks**

To conclude, this study has explored the factors that affect PPP contract management, to address the question whether the Ghanaian public sector has the ability to achieve post-



contractual balance and examine its effects on supplier performance. It is an attempt to advance our understanding of the various impediments that could possibly impact on public sector efforts to develop post-contractual balance, suggesting that if the public sector fails to achieve post-contractual balance with the private sector, leads to the possibility of failing to get suppliers to deliver functionality and cost savings.

In general, the key lesson that can be taken from the study is that the ability to develop post-contractual balance in a country like Ghana in order to obtain the best value for money could be frustrated by power and other external and internal environmental factors. As a result, a useful lesson from this study, which concurs with previous studies, is that both policy makers and governments in developing countries should exercise caution in their optimism that they are capable of achieving post-contractual balance with their international private partners in the manner asserted in the TCE literature. Lastly, as most of the empirical research in the PPP literature has focused on developed countries, we believe that PPP practice in developing countries is a promising research area and that further work would provide more understanding of the impediments to bilateral balance in developing countries.

Accordingly, this study concludes that the ability of the public sector to successfully create a balance is greater when it is able to create a favourable pre-contractual power relationship, and has a competent and capable negotiation team. In the absence of these conditions, the public sector will struggle to develop post-contractual balance with the private sector.

## **APPENDIX A.**

### **Key Research Questions and Interview Guide**

#### **Part A Personal Details**

1. Name.....
2. Ministry /Department/Organisation.....
3. Position/ role.....
4. Address.....  
.....
5. Tel no.....
6. E-mail.....

**IMPORTANT: In each part of the interview schedule define the terms of the concepts to the interviewees before the questions are administered.**

#### **Information on Qualifying Variables**

Sunk and Switching Costs refers to the total cost of previous specialised investment to support a relationship that will be written off if the transaction is terminated or ends.

Switching Cost refers to the cost of transferring from one supplier to another including penalties and fines on one hand and the cost of engaging a new partner including administrative expenses and legal costs on the other.

1. Is the cost of the assets (physical or knowledge) in the relationship jointly own? If yes how is the underlying assets shared?
2. Is the relationship going to require additional physical and nonphysical specific investments and, if so, in what proportion are these assets going to be contributed by each party?
3. In the case of break-up of the relationship can the assets be transferred to another uses without loss of economic value? What proportion are partners to bear the cost of sunk cost?

## **Key Research Questions and Interview Guide**

### **Personal Details About Interviewees**

1. Name.....
2. Ministry /Department/Organisation.....
3. Position/ role.....
4. Address.....  
.....
5. Tel no.....
6. E-mail.....

### **Information on Qualifying Variables**

Sunk and Switching Costs refers to the total cost of previous specialised investment to support a relationship that will be written off if the transaction is terminated or ends.

Switching Cost refers to the cost of transferring from one supplier to another including penalties and fines on one hand and the cost of engaging a new partner including administrative expenses and legal costs on the other.

- I. Is the cost of the assets (physical or knowledge) in the relationship jointly own? If yes how is the underlying assets shared?
2. Is the relationship going to require additional physical and non-physical specific investments and in what proportion are these assets going to be contributed by each party?
3. In the case of break-up of the relationship in what proportion are partners to bear the cost of sunk cost?

## **Part B. Pre-contractual Power Relations-Water management contract:**

### **Ghana Telecom**

1. In your view what were the driving forces of GT to go ahead to form a partnership with TMP to manage the water supply service on its behalf?
2. In what ways would GT have suffered operationally or strategically (ie ability to supply water to the people) if TMP withdraws from the relationship? What were the specific problems GT would have suffered if the contract had not been signed? Explain.
3. What was the main goal of your company in the relation and how does that impact on the pre-contractual negotiations with TMP over contract terms? Could those aims have made TMP more powerful during the negotiation?

### **Scarcity**

1. To what extent did was your choice of managing the water restricted by external and internal demands of the water problems. How has that affected the choice of suppliers to form the partnership?
2. How readily were other equal qualified suppliers available to you in relation to the your invitation to submit bids?
3. Is the supply base restricted? What is the nature and characteristics of the supply market and how did that affect the competitive objectives?

### **Information**

1. In what ways was information about the telecom project and that of the supplier assisted or hampered you in planning your negotiation strategy? Was the information available? Are the relevant details of the contract shared?
2. How effective was the information you had concerning the telecom contract and supply market helped in planning your negotiation strategy?
3. Is there unlimited access to critical information during the contract execution?
4. To what extent were the access to and the quality of information on TMP management activities helped in your monitoring the performance of the company?

### **Part C GT-Resource and Capability of the Negotiation Team**

**Resources and capability of negotiation team:** This is referred to as bargaining skill of a buyer or a supplier negotiation team and the degree of intelligent interaction between them during contract negotiations.

1. To what extent was your procurement department play in your management contract with your public sector company?
2. Explain how your negotiation team prepared for the negotiation.
3. To what extent was the attributes of the negotiation team helped in your negotiation in specific areas in qualification, training, experience, expertise/knowledge?
4. To what extent were the capabilities of your negotiators in terms of independence and professional judgement and management support?
5. From the benefit of hindsight did the negotiation team properly match the resource and capability of the TMP? Explain.
6. To what extent was the performance of your team in terms of extracting concessions from the AVRL team? Specify and explain. If no, explain the difficulties of the team
7. What areas regarding the negotiation team you raised you think should be improved

### **Other Contract Management Issues: Monitoring and Supervision**

1. There a system of monitoring performance of the private sector and ensuring standards? If yes, how successful was it?
2. Is there a system of monitoring performance of the service provider? How do you go about that and was there any problem with the arrangement?
3. How is open is the communication lines between your outfit and the World Bank and the Ghana Water Company

### **E. Contractual Balance Determination.**

1. In what ways was risk shared by GWCL and AVRL when designing the contract? Explain.
2. In your view, what formal provisions (ie rewards, sanctions, information sharing) in the contract exist to facilitate or encourage designing of balanced contract? Explain.

### **Supplier Performance: The public sector's satisfaction with the supplier's**

1. Was there a clear set of performance targets set for evaluating monthly and yearly performance of suppliers? Yes/No. Explain
2. How far has the service provider fulfil the contract obligations? Yes/No Explain.
3. How were the services provided by the service provider contributed to the realisation your organisation goals?

4. The donor agencies state that they were supporting the water sector financially and technically, so why has not this ended up with improved services?

5. Is there any other issues of importance in relating to the pre-contractual negotiations and implementation that I have not touched which you would like to highlight?

Thank you for your time and co-operation.

## **Part 2 Pre-contractual Power Relations-Water management contract:**

### **TMP (Supply-side)**

#### **Utility**

How do you assess the driving forces of your company to take this management contract with GT decision to manage the water supply service in Accra?

2. What ways would your company have suffered operationally or commercially to support the survival of your business operations? (ie criticality to company and value of transaction to overall turnover)

3. What were the specific problems your company would have faced if the contract had not been signed?

4. To what extent was the water contract to the overall profitability and survivability of your company? How has that impacted on your dependence or otherwise on GT contract to the survivability of the company? How had that influence your bargaining strength during the contract negotiation?



### **Scarcity**

1. To what extent were alternative sources of business to support your operational or commercial objective? How has that affected your options to sign the contract?
2. Do you have many business opportunities besides the Ghana telecom contract?
3. What buyer's choices were available to your company regarding the signing of the contract?

### **Information:**

1. In what ways was information about the water project and buyer market assisted or hampered you in planning your negotiation strategy? Was the information readily available and shared?
2. How effective was the information you had concerning the contract helped in planning your negotiation strategy?
3. Is there unlimited access to critical information during the contract execution?
4. To what extent were the access to and the quality of information on TMP management activities helped in your monitoring the performance of the company?

### **Part C. Resource and Capability**

To what extent was your sales/marketing team play in your management contract with your public sector company?

2. Explain how your negotiation team prepared for the negotiation.

3. To what extent was the attributes of the negotiation team in terms of helped in your negotiation with specific factors of qualification, training, experience, expertise/knowledge
4. Can you specify the special qualities of your negotiation members you consider provided you with competitive advantage in your negotiation?
6. What was the level of management support and extent of capabilities of the negotiation team.
5. From the benefit of hindsight did the negotiation team properly match the resource and capability of the GT? Explain.

#### **E. Contractual Balance:**

1. In what ways was risk shared by TMP and GT in the contract? Explain.
2. In your view, what is your assessment of the degree of balance in the contract design? Explain.

#### **Supplier Performance: Meeting Contract Provision**

1. Was there a clear set of performance targets set for evaluating monthly and yearly performance?
2. How far has your company (TMP) been able to meet those targets or fulfil the GT expectations?
3. Is there any other issues of importance in relating to the pre-contractual negotiations and implementation that I have not touched which you would like to highlight?

Thank you for time and co-operation.

## **THE SECOND CASE: THE WATER CONTRACT.**

### **Part B**

#### **GWCL: Pre-contractual Power Relations-Water management contract: Buyer**

##### **Utility**

1. In your view what were the driving forces of GWCL to go ahead to form a partnership with AVRL to manage the water supply service on its behalf?
2. In what ways would GWCL have suffered operationally or strategically (ie ability to supply water to the people) if AVRL withdraws from the relationship? What were the specific problems GWCL would have suffered if the contract had not been signed? Explain.
3. What was the main goal of your company in the relation and how does that impact on the pre-contractual negotiations with AVRL over contract terms? Could those aims have made AVRL more powerful during the negotiation?

##### **Scarcity:**

1. To what extent did was your choice of managing the water restricted by external and internal demands of the water problems. How has that affected the choice of suppliers to form the partnership?

2. How readily were other equal qualified suppliers available to you in relation to the your invitation to submit bids?
3. Is the supply base restricted? What is the nature and characteristics of the supply market and how did that affect the competitive objectives?

### **Information**

1. In what ways was information about the water project and that of the supplier assisted or hampered you in planning your negotiation strategy? Was the information available? Are the relevant details of the contract shared?
2. How effective was the information you had concerning the water contract and supply market helped in planning your negotiation strategy?
3. Is there unlimited access to critical information during the contract execution and how did that impacted on your efforts to control the performance of the service provider?
4. To what extent were the access to and the quality of information on AVRL management activities helped in your monitoring the performance of the company?

### **Part C GWCL-Resource and Capability of the Negotiation Team**

**Resources and Capability of Negotiation team:** This is referred to as bargaining skill of a buyer or a supplier negotiation team and the degree of intelligent interaction between them during contract negotiations.

1. To what extent was your procurement department play in your management contract with your public sector company?
2. Explain how your negotiation team prepared for the negotiation.
3. To what extent was the attributes of the negotiation team helped in your negotiation in specific areas in qualification, training, experience, expertise/knowledge?
4. To what extent were the capabilities of your negotiators in terms of independence and professional judgement and management support?
5. From the benefit of hindsight did the negotiation team properly match the resource and capability of the AVRL? Explain.
6. To what extent was the performance of your team in terms of extracting concessions from the AVRL team? Specify and explain. If no, explain the difficulties of the team
7. What areas regarding the negotiation team you raised you think should be improved?

### **Other Contract Management Issues: Monitoring and Supervision**

1. There a system of monitoring performance of the private sector and ensuring standards? If yes, how successful did it work?
2. Is there a system of monitoring performance of the service provider? How do you go about that and was there any problem with the arrangement?

3. How is open is the communication lines between your outfit and the World Bank and the Ghana Water Company.

### **E. Contractual Balance:**

1. In what ways was risk shared by GWCL and AVRIL when designing the contract? Explain.

2. In your view, what formal provisions (ie rewards, sanctions, information sharing) in the contract exist to facilitate or encourage designing of balanced contract? Explain.

### **Supplier Performance: The public sector's satisfaction with the supplier's**

1. Was there a clear set of performance targets set for evaluating monthly and yearly performance?

2. How far has the service provider fulfil the contract obligations? Explain.

3. How were the services provided by the service provider contributed to the realisation your organisation goals?

4. The donor agencies state that they were supporting the water sector financially and technically, so why has not this ended up with improved services?

5. Is there any other issues of importance in relating to the pre-contractual negotiations and implementation that I have not touched which you would like to highlight?

Thank you for your time and co-operation.

## **Part B Pre-contractual Power Relations-Water management contract:**

### **AVRL (Supply-side)**

#### **Utility**

How do you assess the driving forces of your company to take this management contract with GWCL decision to manage the water supply service in Accra?

2. What ways would your company have suffered operationally or commercially to support the survival of your business operations? Explain.
3. What were the specific problems your company would have faced if the contract had not been signed?
4. To what extent was the water contract to the overall profitability and survivability of your company? How has that impacted on your dependence or otherwise on GWCL contract to the survivability of the company? How had that influence your bargaining strength during the contract negotiation?

#### **Scarcity**

1. To what extent were alternative sources of business to support your operational or commercial objective? How has that affected your options to sign the contract?
2. Do you have many business opportunities besides the Ghana water contract?
3. What buyer's choices were available to your company regarding the signing of the contract?

**Information:**

1. In what ways was information about the water project and buyer market assisted or hampered you in planning your negotiation strategy? Was the information readily available and shared?
2. How effective was the information you had concerning the contract helped in planning your negotiation strategy?
3. Is there unlimited access to critical information during the contract execution?
4. To what extent were the access to and the quality of information on AVRIL management activities helped in your monitoring the performance of the company?

**Part C: Negotiation Resources and Capabilities**

1. To what extent was your sales/marketing team play in your management contract with your public sector company?
2. Explain how your negotiation team prepared for the negotiation.
3. To what extent was the attributes of the negotiation team in terms of helped in your negotiation with specific factors of qualification, training, experience, expertise/knowledge
4. Can you specify the special qualities of your negotiation members you consider provided you with competitive advantage in your negotiation?



6. What was the level of management support and extent of capabilities of the negotiation team.
5. From the benefit of hindsight did the negotiation team properly match the resource and capability of the GWCL? Explain.

### **E. Contractual Balance:**

- 1.what types of risk you considered before signing the contract?
- 2.In what ways was risk shared by AVRL and GWCL in the contract? Explain.
- 3.In your view, what is your assessment of the degree of balance in the contract design? Explain and justify.

### **Supplier Performance: Meeting Contract Provision**

- 1.Was there a clear set of performance targets set for evaluating monthly and yearly performance?
- 2.How far has your company (AVRL) been able to meet those targets or fulfil the GWCL expectations?
3. How do you explain your performance?
- 3.Is there any other issues of importance in relating to the performance both at company level and government level I have not touched which you would like to highlight?

Any other relevant information you want to add or comments you want to make.

Thank you for time and co-operation.

## **World Bank**

1. The shift to public sector participation has been advocated to increase management efficiency demands an enabling working environment so managers can achieve efficiency goals and targets. Has his ended up with improved services? If not, why?
2. How has the World Bank integrated measures in the management contract design to ensure a level playing ground is created for an inter-dependent relationship to exist between the buy-side and the supplier side?
3. It was said that the World Bank support to PPP idea and the policy to make Ghana use the private sector to manage its key utility sectors is one of the main obstacles to the consideration of alternative ways of managing the sector.
4. Is the World Bank conditionalities most significant to the development of a mutual inter-dependent relation? If not, then what are the most significant problems that created for the Ghanaian public sector?
5. The World Bank state that they were supporting the Ghanaian water and telecom sector financially and technically, so why have these not this ended up with improved services from the service providers?
6. Any other relevant information you want to add or comments you want to make.

Thank you for time and co-operation.

## **Government Ministers**

1. How do you assess the performance of the public sector both in the GT and GWCL in the management contract?
2. Could the management contract be a kind of testing in practical local conditions to develop into a more “involved form” of private sector participation.
3. What were the main considerations of the government to seek a private professional management services to manage the two public companies? How has that contributed to the bargaining strength with the service providers?
4. The introduction of management contract of PPP has been practiced over time how do you assess the management contract of PPP as one that created equal opportunity for the public sector to get a better deal.
5. Any other relevant information you want to add or comments you want to make.

Thank you for time and co-operation.

Note: Ask for explanations that may contradict evidence from other sources.

## APPENDIX B

### Appendix 2: Coding of the Variables

Code	Particulars of Attribute Variable	
utilP	Partners perception of the transaction to its operational needs Partners perception of the transaction to its strategic /commercial objectives	Utility
ScaP	Availability of alternatives	Scarcity
TimeP	Time essence and sensibility	Scarcity
infoP	Accessibility of key information Open door policy and easy access to records Frequency of reporting service providers performance	Information
Rescap P	Partners experience, skills and capabilities in contract negotiation	
BalAssets	Investments in fixed assets and non-physical assets. Proportion of risk transferred from the public sector to the service providers	Risk sharing/allocation
Conflex	Flexibility in response to future events as they relate to the contract management Equal opportunity for contract adaptation and negotiation for genuine post-contractual negotiations	Balance
ConItive	Equal incentive and risk	
ServPerf		
PostCon Bal	Balance of contract in risk and incentives	

Key: utilP: Utilities of both contracting party and service providers

ScaP: Scarcity

TimeP. Time as it relates to concluding the contract

InforP: Information

Rescap P: Resource and capabilities

BalAssets: Proportion or risk transferred from the government to private service providers

Conflex: contract flexibility and re-negotiation

ConItive: Incentive contracting

ServPerf: Service performance

PostConBal

### Appendix 3: Indications and Measurement for public sector

Code	Indicator		PostConBal	ServPerf:
UtilP	Public sector operational and strategic importance		+	
ScaP	Suppliers scarcity		+	
TimeP	Time sensitive		+	
InfoP	Transparency and information sharing		+	
Rescap P	Public sector resources and capabilities deplored Experience, skills and education		+	
BalAssets	Public sector bearing all the risk in specific assets		+	
Conflex	Contract rigidity		+	
ConItive	Contract with incentive mechanism		-	
ServPerf	Meeting government's minimum expectation of performance		-	

+/- positive impact or negative impact

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